LIBRARY
SUPREME COURT, U.S.

No. 715 39

Office - Supreme Court, U. S.
FILED
APR 14 1953
HAROLD B. WILLEY, Clerk

United States Supreme Court

October Term, 1952 / 1953

ANTHONY WILKO,

Petitioner,

vs.

JOSEPH E. SWAN, ET AL,
individually and doing business under the firm name and style of Hayden Stone & Co.

Defendants-Respondents,

and

HAVEN B. PAGE,

Defendant.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

HENRY E. MILLS
Counsel for Petitioner

20 Pine Street,
New York 5, N. Y.

INDEX

	PAGE
OPINIONS BELOW	4
JURISDICTION	5
QUESTIONS PRESENTED	5
STATUTES INVOLVED	5
STATEMENT OF FACTS	6
SPECIFICATION OF ERRORS TO BE URGED	7
REASONS FOR GRANTING THE WRIT	12
CONCLUSION	18
APPENDIX:	19
A Reprint of excerpts from Arbitration Agreement of American Arbitration Association	1–2

Cases Cited

PAGES

American Almond Products vs. *Consolidated Pecan Sales Co., Inc.*, 144 Fed. 2d, 448, 154, A. L. R. 1205 (C. A. 2d—1944) 16

United Fuel Gas Co. vs. *Columbian Fuel Corp.*, 165 Fed. (2d) C. C. A. 4 16

Donahue vs. *Susquehanna Collieries*, 160 Fed. 2d 661 (C.A. 3—1947) 11

Jefferson Lake Sulphur Company vs. *Walet*, 104 Fed. Supplement 20 (1952) Decision of District Court confirmed by Circuit Court of Appeals (5 C. A.) (1953) 10–15

Kaiser-Frazier Corp. vs. *Otis & Co.*, 195 Fed. 2, 838-844.....

Shanferoke Coal & Supply Corp. vs. *Westchester Service Corp.*, 70 Fed. 2d 297, 299 (C.A. 2d 1934) affirmed, 293 U.S. 449 (1935) 16

Burchell vs. *Marsh et al*, 58 U.S. 344..... 13

Wilko vs. *Swan*, S. D. N. Y. 1952 C.C.H. Fed. Securities Laws Service Par. 90, 531.....herein

Statutes

U. S. Code annotated Title 28 Sections 1252 and 1254 (Judiciary & Judicial Procedure)..... 5

U. S. Code annotated Title 15, Chapter 2a, Sections 77k, 771-2 and 77n, 77p. 77v(a) (Securities Act of 1933).....5–8–9–11–13

U. S. Code annotated Title 15, Chapter 2b—Sections 78g, 78h, 78i, 78k, 78o-3, 78p-b, 78q, 78cc and 78dd (Securities Exchange Act of 1934).....10–11

U. S. Code annotated Title 9, Sections 2, 3, 10 and 11 (Federal Arbitration Act of 1925).....5–6–8

New York Arbitration Law Civil Practice Act ¶1462, ¶1462a

Legislative History

	PAGES
Sen. Rep. No. 47, 73d Cong., 1st Sess. (1933), pp. 6-7	12
H. R. Rep. No. 85, 73d Cong., 1st Sess. (1933):	
p. 2	12 of record herein
pp. 9-10	12 of record herein
H. R. Rep. No. 96, 68th Cong., 1st Sess. (1924), p. 2	
(See appropriate references in Transcript of record herein)	

Articles, Texts, Etc.

American Arbitration Association, Commercial Arbitration Rules, Rule 30, clause recommended by arbitration for insertion in all Commercial Contracts ..... Appendix pages 1–2

Chamber of Commerce of the State of New York, *Handbook and Guide to Arbitration under the New York and United States Arbitration Statutes* (1932):

pp. 4-6 .....

p. 23 .....

pp. 33-34 .....

p. 39 .....

Cohen and Dayton, *The New Federal Arbitration Law*, 12 Va. L. Rev. 265, 281 (1926) .....

Frank, *Courts on Trial* (1949), pp. 376-377 .....

Jacquin, *Arbitration on the Big Board*, Arbitration in Action, vol. 1, no. 2, p. 5 (1943) .....

Loss, *Securities Regulation* (1951), pp. 1011-1029, 1074-1077 ..

Moore, *Federal Practice* (2d ed. 1951), vol. 5, ¶43.08 .....

New York Stock Exchange Arbitration Agreement Appendix page 1

Stone, *Justice Weighs Bulls and Bears*, Investment Dealers' Digest, Jan. 28. 1952, p. 20 .....

(1) No page reference given for statutes, legislative documents and articles, texts, etc., presumed to be at disposal of the Court.

United States Supreme Court

October Term, 1952

No. .....

ANTHONY WILKO,

Petitioner,

vs.

JOSEPH E. SWAN, ET AL,
individually and doing business under the firm name and style of Hayden Stone & Co.

Defendants-Respondent,

and

HAVEN B. PAGE,

Defendant.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit, entered in the above entitled case on January 15, 1953.

Opinions Below

The opinion of Judge Goddard of the United States District Court for the Southern District of New York herein is reported in 107 Fed. Supplement 75. The opinion of the Circuit Court of Appeals herein is reported in 201 Fed. 2d 439.

Jurisdiction

The judgment of the Circuit Court of Appeals for the Second Circuit was entered on January 15, 1953. The jurisdiction of this Court is invoked under 28 U. S. Code Annotated, Sections 1252 and 1254.

Questions Presented

The questions presented in this case are very important and affect virtually all members of the securities professions and officers and employees of all nationally registered securities exchanges as well as virtually every buyer and seller of securities throughout the United States and are briefly:

(1) Whether Sections 77 l and 77 n of the Securities Act of May 27, 1933 as amended (Title 15, Chapter 2a) U. S. Code Annotated (C38- Title 1, 48 Stat. 74) render compulsory arbitration clauses contained in fine print at the end of customer's agreements signed between petitioner (customer) herein, and respondents (brokerage house) invalid and not binding upon petitioner (customer)

and

(2) Whether the Federal Arbitration Act of 1925, predating the Securities Act of 1933 by some eight years renders the non-waiver provisions of the latter act invalid?

and

(3) Whether an arbitration can be supervised by the District Court in a manner contrary to settled law and Section 77n of the Securities Act of 1933 as Amended. (Title 15, Chapter 2a) U. S. C. A. (C38—Title 1, 48 Stat. 74)?

Statutes Involved

The pertinent statutory provisions are as follows:

(1) Sections 12 (2) and (14) of the Securities Act of 1933, and Sections 3 and 10 of the Federal Arbitration Act of 1925.

Statement of Facts

(1) Petitioner herein was a customer of the firm of Hayden Stone & Co., members of the New York Stock Exchange, and respondents herein. Petitioner's complaint herein is dated January 14, 1952 (see pages 2-4 inclusive) of the transcript of record herein, and alleges that:

(2) Respondents sold to petitioner 1,600 shares of the common stock of Air Associates, Inc., a corporation of the State of New Jersey on or about January 17, 1951, and petitioner paid respondents Hayden Stone & Co. therefor the sum of $29,517.54. That on or about February 2 and 3, 1951, petitioner sold through the respondents herein the 1,600 shares abovementioned on the New York Curb Exchange for a total price of $25,628.61, thereby incurring a loss of $3,888.88.

(3) That the above purchase and sale were made by the use of the means and instrumentalities of interstate commerce, including the facilities of the New York Curb Exchange, a nationally registered securities exchange, the United States Mails, and that the original sale to the petitioner herein resulted from communications to the petitioner by the respondents herein, which included untrue statements of fact, and omissions to state material facts necessary to make the respondent's statements not misleading, in the light of the circumstances under which these statements were made.

(4) That respondents herein moved on February 29th, 1952 in the U. S. District Court for the Southern District of New York to stay all proceedings herein pursuant to Title 9. U. S. C. Sec. 3, (1950 Supplement) until an arbitration could be had as provided for in the last clause of the customer's agreement entered into between petitioner and respondents on May 2, 1950.

(5) The Securities & Exchange Commission was granted permission by the United States District Court to intervene herein as amicus curiae. The Securities & Exchange Com-

mission so intervened and submitted briefs as well as oral arguments supporting petitioner's contentions and allegations herein.

(6) After the trial of this action in the United States District Court for the Southern District of New York, Judge Henry W. Goddard handed down a decision on May 23, 1952, denying respondent's motion for a stay pending arbitration and an order to this effect was entered on June 11, 1952.

(7) Respondents filed a notice of appeal to the Circuit Court of Appeals for the 2d Circuit on June 18, 1952.

(8) While petitioner stipulated the correctness of the transcript of record as submitted to him on July 24, 1952, respondents failed to amend this record so as to show that on August 28, 1952, Judge Edelstein of the United States District Court for the Southern District of New York again denied a motion of respondents for a further stay of all proceedings herein pending a hearing of the appeal in the Circuit Court of Appeals for the 2d Circuit.

(9) After a further intervention by the Securities & Exchange Commission in support of plaintiff's (petitioner's) contentions and the submission of briefs and oral arguments, the Circuit Court of Appeals in a *divided opinion* handed down a decision on January 15, 1953, reversing Judge Goddard, and remanding the case to the U. S. District Court for further proceedings.

Specification of Errors to be Urged

The Court of Appeals erred:

(1) In holding that there was no civil liability upon respondents for their fraud upon petitioner misrepresentation of material facts and omissions to state material facts necessary to make respondent's statements not misleading in inducing petitioner to purchase 1,600 shares of the common stock of Air Associates, Inc., on or about January 17, 1951. This serious fraud has been completely ignored

both by the majority of the Circuit Court of Appeals and by Respondents and their Counsel.

(2) In holding that the clause in the customer's agreement compelling the customer-petitioner to submit to compulsory arbitration in the event of a dispute is not one waiving compliance with the Securities Act of 1933, of which Section 77n thereof reads as follows:

> "Any condition, stipulation or provision binding any person acquiring any security to waive compliance with any provision of this sub-chapter, and of the rules and regulations of the Commission shall be void."

(3) In holding that both Sections 12 (2) and 14 of the Securities Act of 1933 are merely permissive and do not require compliance on the part of respondents herein. This holding is in defiance of the provisions of the Securities Act of 1933, as provided in Section 12 (2) and Section 14 thereof, which respondents admit in the customer's agreement are valid and binding upon them, by using the words Securities and Exchange Act of 1934 and present and future acts amendatory thereof or supplementary thereto. Congress does not enact permissive legislation, except in rare instances. If the non-waiver provisions above named were and are merely permissive there would have been no object on the part of Congress in enacting them.

(4) In holding that under the Federal Arbitration Act of 1925 (an act antedating the Securities Act of 1933 by nearly 8 years) permits arbitrators to act outside their status as laymen, as lawyers, judges and jurors in spite of their lack of professional preparation and experience in the practice of law.

(5) In assuming that arbitrators would be bound to decide this dispute in accordance with the provisions of Section 12 (2) of the Securities Act of 1933. Both the

---

[1] See photostatic copy of customers agreement Exhibit C in Appendix.

majority of the Circuit of Appeals and opposing counsel have failed to consider the self-interest of the arbitrators particularly, if the arbitration were to be conducted by the Arbitration Committee of the New York Stock Exchange, few, if any, of whose members are lawyers and all of whom have a direct personal interest in increasing the income and assets of their fellow members of the New York Stock Exchange, and in reducing the liabilities and disbursements of such members. No evidence was adduced by respondent's at any time to prove that the members of panels of other arbitration agencies are not just as biased in their approach to disputes between wealthy stock exchange houses and relatively poor customers. The entire customer's agreement involved herein was obviously worded by shrewd attorneys, to achieve exculpation for their clients, to circumvent federal statutes and settled law, and to obviate compliance with legal mandates to the contrary.

(6) In ruling (by the majority) that the Court could not find in the purpose or in the language of the 1933 Act a policy argument strong enough to over-ride the policy of the Arbitration Act (enacted some eight years before the Securities Act of 1933) and further that "If Congress had intended to forbid arbitration in a suit based on Section 12 (2), we believe that it would have expressed such intent."

(7) In holding that the absence of Haven B. Page from the arbitration agreement did not enable the plaintiff to escape his contract to arbitrate. There is no privity of contract between the aforesaid Page and the petitioner herein. The Supreme Court of the United States may note from the transcript of the record submitted herewith that Haven B. Page, was not an appellant to the Circuit Court of Appeals herein and is specifically and purposely segregated as a *defendant* herein.

(8) In holding that the District Court has the authority to supervise the arbitration proceeding to safeguard petitioner's rights under the 1933 Act. This erroneous judgment is so conspicuous that it is almost unbelievable to find it in

the opinion of even a divided section of one of our Federal Courts.

(9) In holding that a ruling in a case involving similar statutes (15 U. S. C. 78p (b) and 78AA) in the United District Court for the Eastern District of Louisiana (*Walet* vs. *Jefferson Lake Sulphur Company* 104 Fed. Supplement 20) was not in conflict with the Circuit Court's ruling in the instant case. Respondents in paragraph 2 of the customer's agreement under consideration bind themselves "to comply with all transactions made by you are to be subject to" * * * the provisions of the Securities Exchange Act of 1934 and present and future acts amendatory thereof or supplemental thereto and to the rules and regulations of the Securities and Exchange Commission including the provisions virtually identical with Sections 77n and 77l of the Securities Act of 1933 quoted supra. This decision of the District Court has recently been upheld by the United States Court of Appeals for the Fifth Circuit which held specifically that the "Appellee, * * * should not be held to have waived the benefits of Section 16 (b) "of the Securities Exchange Act of 1934," "which holds that the Federal Courts shall have exclusive jurisdiction of violations of this chapter * * *."[1]

---

[1] *See also* the American Arbitration Association which explicitly provide that *"the Arbitrator shall be the judge of the relevancy and materiality of the evidence offered and conformity to legal rules of evidence shall not be necessary."* (Emphasis supplied)—See Appendix—Exhibit B.

It is highly significant that respondents never cited these controlling rules of arbitration. There is no court decree that can obviate these barriers to impartial arbitration. Respondents are afraid to face courts and juries in the forums provided under clear and categorical statutory provisions for the protection of the petitioner.

Under the Federal Arbitration Act (9 U.S.C.—Sections 10 and 11, the Court's power to review an award is extremely limited in scope.

Judge Goddard said in his opinion in the District Court that:

"Arbitration ought not to prevail where it would clearly defeat the *urgent* policy considerations as expressed by Congress in the Securities Act. In view of the informality of the arbitration proceedings and the restricted court review, see United Fuel Gas vs. Columbian Fuel Corp., 165 Fed. (2d) 746 C.C.A. 4; Burchell vs. Marsh et al, 58 U.S. 344; Title 9, U.S.C. and Sections 10, 11 there is no certainty that the rights of the purchaser accorded him by Section L would be wholly protected in an arbitration proceeding."

In the United Fuel Gas Co. case, the Court held that "Parties cannot by contract oust federal courts of their statutory jurisdiction."

(10) In holding that the Securities Act of 1933 does not evidence a public policy which forbids referring the instant controversy to arbitration.[1]

C. C. A.'s Judge Clark held that "such a course would have neither a usual or a safe and proper method of draftsmanship. The language chosen is broad and general as befits the intent. It seems wholly adequate and effective to safeguard the investor against loss of his right of suit under the act and the important burden of proof which it grants in his favor." And later * * * "Because I believe important rights under this notable first of a series of famous Acts for the benefit of the investing public should not be capable of nullification by long fine-print restrictions of the broker's devising, I think the ruling below wise and beneficent. I would affirm."

Kaiser-Frazier Corp. vs. Otis & Co., 195 Fed. 2d 838, 843-4, 6, the Court declared at page :

> "the obvious purpose of the Congress in its enactment was the protection of the investing public.

The Securities and Exchange Commission on pages 23-4 of their brief on appeal to the C.C.A. for the 2d Circuit state:

> "(1) That respondents herein present a tortuous argument to the effect that the phrase 'compliance with' applies to the broker and not to the customer. It is elementary law that no one except the contracting party himself can waive his contractual rights" and further on the same page (23) of the brief of the Securities and Exchange Commission to the Circuit Court of Appeals herein; the Commission says: "Section 12(2) of the 1933 Act does require that the fraudulent seller be responsible for the wrong and

[1] In holding that the ruling of the C. C. A. for the Third Circuit in the case of *Donahue* vs. *Susquehanna Collieries Co.*, 160 Fed. 2d 661 C. C. A. 3 (1947) was relevant herein. The Supreme Court's attention is drawn to the fact that case arose from transactions in *coal*, and from legislation pre-dating the Securities Act of 1933 and not from transactions in *securities* for which Congress has made special provisions in Section 771 and 77n of the Securities Act of 1933.

the injury to the purchaser in a court proceeding. . . . Waiver of customer's remedy is thus in a very material respect a waiver of the requirements of Section 12(2) and citing the Kaiser-Frazier—Otis case supra, the General Counsel of the SEC says: "Section 14 is broad in scope and sufficiently broad, we believe, to apply to the waiver which Appellants sought to obtain from the instant plaintiff."

(12) Reasons for Granting the Writ.

The Circuit Court of Appeals has decided an important question of Federal Law which has not been, but should be settled by this court.

The writ sought herein should be granted because there are direct conflicts with decisions in other Circuit Courts of Appeals. And is probably in conflict with the applicable decisions of this Court. The majority of the C. C. A. herein have so far departed from the accepted course of judicial proceeding as to call for an exercise of the Supreme Court's power of supervision.

One of the prime purposes of the certiorari jurisdiction is to bring about uniformity of decisions within the Federal Courts and particularly within the various Circuit Courts of Appeals.

No claim or evidence was ever adduced by respondents herein to the effect that they had ever submitted the customers' agreement herein to either the Securities and Exchange Commission or the New York Stock Exchange for consideration and approval. The Securities and Exchange Commission is charged by law with the administration of certain statutes that have become settled law. It maintains an interpretative division to render opinions to the public and the legal profession.

There is a conflict between the ruling of the majority of the C. C. A. herein and the expressed intent of Congress at the time of enacting the remedial legislation.

Judge Goddard's opinion of May 25, 1952 citing holds clearly to the opposite of respondents the clear expression

of the intent of the Senate and the House of Representatives at the time the Securities Act of 1933 was being considered in Washington.

Judge Goddard made it crystal clear that the intent of Congress was that "the provisions of the Securities Act of 1933 should be strictly complied with so that the purchaser of securities would be protected as fully as possible" and that Congress made no change in Section 771 of the 1933 Act at any later date.[1]

Judge Goddard further made it clear that "many purchasers of securities would not hesitate to sign a printed form in small type which includes a provision for arbitration, thereby waiving the remedies provided by the Securities Act of 1933, particularly as few purchasers are aware of the provisions of the Securities Act" of 1933. "A collateral agreement of this nature would nullify the Act's basic purpose and allow the purposes of Congress to be circumvented."

Judge Goddard further said:

> "In the Senate report on the bill it was said:
>
> It is now *imperative* that the Federal Government shall adopt measures looking to the protection of the purchasers of securities in interstate commerce." (Emphasis added) Senate Report No. 47, 73d Cong. 1st Sess. 1933 Page 2.
>
> "The House Committee report stated:
>
> Unless responsibility is to involve merely paper liability it is necessary to throw the burden of disproving responsibility for reprehensible acts of omission or commission on those who purport to issue statements for the public's reliance. The responsibility imposed is no more than nor less than that of a trust. It is a responsibility that no honest banker and no honest business man should seek to avoid or fear. *To impose a lesser responsibility would*

[1] See pages 27-29 from Transcript of Record.

nullify the purposes of the legislation." H. R. Rep. No. 85, 73d Cong. 1st Sess. (1933) pages 9-10.

Judge Goddard further says:

"In the light of this background of Congressional purpose, the liabilities provision of Section 77l and the anti-waiver provision of Section 77n were enacted, and they must be construed accordingly and may not be disregarded. The serious concern which the Congress had for the protection of the investor is evident. It provided a court remedy for the purchaser, and it was deemed essential that a part of the burden of proof should rest on the seller."

There is a conflict between the majority of the C. C. A. for the 2d Circuit and its minority member Judge Clark herein.

The highest Court of this country is respectfully referred to Judge Clark's dissenting opinion in which he holds correctly that "The role of the burden of proof concept is to canalize and control the evidence; it may often be the decisive factor in the case"—and infra—"the arbitrators will act according to their business background and there will be no way of checking what they do." * * * "So what is most desirable in the ordinary arbitration becomes a clear loss of a statutory right here." (See page 52 of Transcript of record herein.)[1]

There are conflicts between the majority opinion of the C. C. A. for the 2d Circuit and decisions reached in the following cases in the same and other circuits:

(1) With the Second Circuit itself in the cases of American Almond Products vs Consolidated Pecan Sales Co., Inc., 144 Fed 2d, 448 et seq, 154 A. L. R. 1205, C. A. 2d—1944

Shanferoke Coal and Supply Corp vs Westchester Service Corporation, 70 Fed 2d 297, 299 (C. A. 2d 1934) affirmed, 293 U. S. 449, (1935)

---

[1] . . . "The Burden of Proof has been characterized as a matter of Substance." See Moore's Federal Practice (2d ed. 1951) Volume 5 ¶43.08 and cases cited therein.

(2) With the Third Circuit in the case of Donahue vs. Susquehanna Collieries Co. 138 Fed 2d 3 (C. A. 3—1943).

(3) With the Fourth Circuit in the case of United Fuel Gas Co. vs Columbian Fuel Corp., 165 Fed (2d) 746 (1948)

(4) With the Fifth Circuit in the case of Jefferson Lake Sulphur Company vs Walet 104 Fed Sup. 20, (1952); Cf. C. A. 5 Fed 2d (1953) decision handed down March 1953—as yet unreported.

There is a direct conflict in the decision of the majority of the C. C. A. for the Second Circuit and the decision of Judge Goddard in the United States District Court for the Southern District of New York. This is clearly evidenced by the filing of the appeal of the respondents herein.

The importance of the questions involved cannot be overestimated. Efforts to enforce compulsory arbitration affect nearly everyone who transacts business on nationally registered exchanges either as a customer or a broker. It affects the officers and employees of the exchange themselves as well as the staffs of Federal administrative agencies. This case does not turn on its own special facts or on consequences peculiar to the particular parties herein. It was considered of great importance to the Securities and Exchange Commission and sufficiently so to bring intervention as amicus curiae in both the District Court and the Circuit Court of Appeals.

The Securities and Exchange Commission in their brief filed with the Circuit Court of Appeals is in accord with Judge Clark and sums the dilemma up cogently and clearly when it says on page 31 of its brief: "It is evident that appellants' proposal subverts the very purpose of arbitration. And if the Court is to assume such detailed supervision, should it not try the case itself without the intervention of arbitration?"

Respondents in their brief on appeal quote excessively from English statutes and decisions. These quotations are

sheer surplusage, if not arrant *red-herrings*, as far as their relevance to the instant case is concerned. There was a revolution in 1776, and English law has been repealed or largely superseded by our own Federal and State statutes and decisions.

Quoting from the relevant paragraph on page 35 of the brief of the Securities and Exchange Commission on appeal to the Circuit Court of Appeals[1,2] we find the following excerpt from the Circuit Court's decision in the case of American Almond Products Co., vs. Consolidated Pecan Sales Co., Inc.,:

> "Arbitration may or may not be a desirable substitute for trials in courts; as to that the parties must decide in each instance. But when they have adopted it, they must be content with its informalities; they may not hedge it about with THOSE PROCEDURAL LIMITATIONS WHICH IT IS PRECISELY ITS PURPOSE TO AVOID. THEY MUST CONTENT THEMSELVES WITH LOOSER APPROXIMATIONS TO THE ENFORCEMENT OF THEIR RIGHTS THAN THOSE THAT THE LAW ACCORDS THEM, WHEN THEY RESORT TO ITS MACHINERY." (Emphasis supplied)

(See opinion by Judge Learned Hand in above case.)

The majority of the Court of Appeals in the Second Circuit and respondent's counsel have specifically ignored the well-known fact that arbitrations are conducted by all the agencies mentioned in the customer's agreement only after the customer has signed an arbitration agreement containing the following or similar clause.

> "THE DECISION OF THE MAJORITY OF THE ARBITRATORS SHALL BE FINAL." (Emphasis supplied.)[3]

---

1 144 Fed. 2d—448, 451, 154 A.L.R. 1205 C.A. 2d—1944.

2 *See also* Judge Augustus Hand's remarks in In Re Canadian Gulf Line, 98 Fed. 2d 711, 714. (C.A. 2—1938.)

3 See Arbitration Agreement New York Stock Exchange, page . See Appendix —Exhibit A, submitted herewith.

The majority of the C. C. A. for the 2d Circuit admits in its opinion herein that "the appeal presents an interesting question of statutory construction said to be of first impression." and admits further:[1]

> . . . "the brief of the Securities & Exchange Commission as amicus curiae . . . makes a strong presentation of the argument in support of Judge Goddard's decision."

The same majority also refers on the same page to Judge Goddard's "carefully reasoned opinion."

Later on the last page of Judge Swans opinion herein, he states "Although the question is not free from doubt, and Judge Goddard's opinion presents a strong argument against the conclusion we have reached . . ."[2]

Petitioner respectfully submits that the dissenting opinion of Judge Clark herein represents the correct ruling in this particular case. Judge Clark says at the beginning of his opinion:[3]

> "Judge Goddard's incisively reasoned opinion D. C. S. D. N. Y. 107 Fed. Supp. 75 and the able supporting arguments of the Securities and Exchange Commission are to me very convincing . . . " and infra . . . It would be vastly unfortunate if" (arbitration) "it became useable as a device to blunt or break social legislation."

To fail to grant the writ of certiorari to the petitioner herein would constitute a long step backward in the enforcement of federal statutes; back to the days before 1933 when the "lambs" were shorn regularly and continuously by the "wolves" of Wall Street.

---

[1] See page 43 of Transcript of record herein.

[2] See page 46 of Transcript of record herein.

[3] See page 51 of Transcript of record herein.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

.....

Counsel for Petitioner.

APPENDIX

Exhibit A

For the arbitration of *future* disputes:—

The American Arbitration Association recommends the following arbitration clause for insertion in all commercial contracts:

STANDARD ARBITRATION CLAUSE

Any controversy or claim arising out of or relating to this contract, or the breach thereof, shall be settled by arbitration in accordance with the Rules of the American Arbitration Association, and judgment upon the award rendered by the Arbitrator(s) may be entered in any Court having jurisdiction thereof.

For the Submission of *existing* disputes:—

We, the undersigned parties, hereby agree to submit to arbitration under the Commercial Arbitration Rules of the American Arbitration Association the following controversy: (cite briefly). We further agree that the above controversy be submitted to (one) (three) Arbitrators selected from the panels of Arbitrators of the American Arbitration Association. We further agree that we will faithfully observe this agreement and the Rules and that we will abide by and perform any award rendered by the Arbitrator(s) and that a judgment of the Court having jurisdiction may be entered upon the award.

Exhibit B.—Copy of page .... of Arbitration Agreement of American Arbitration Association.

Evidence—

The parties may offer such evidence as they desire and shall produce such additional evidence as the Arbitrator may deem necessary to an understanding and determination of the dispute. When the Arbitrator is authorized by law to subpoena witnesses or documents, he may do so upon his own initiative or upon the request of any party. The Arbitrator shall be the judge of the relevancy and materiality of the evidence offered and conformity to legal rules of evidence shall not be necessary. All evidence shall be taken in the presence of all of the Arbitrators and of all the parties except where any of the parties is absent in default or has waived his right to be present.

LIBRARY
SUPREME COURT, U.S.

Office - Supreme Court, U.
FILE
MAY 28 1953
HAROLD B. WILLEY, Clerk

IN THE

United States Supreme Court

October Term, ~~1952~~ 1953

No. ~~320~~ 39

ANTHONY WILKO,

Petitioner,

against

JOSEPH E. SWAN, *et al.*,

individually and doing business under the firm name and style of Hayden, Stone & Co.,

Defendants-Respondents,

and

HAVEN B. PAGE,

Defendant.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR PETITIONER TO RESPONDENTS OPPOSITION BRIEF HEREIN

HENRY E. MILLS,
20 Pine Street,
New York, New York,
Attorney for Petitioner.

RICHARD H. WELS,
551 Fifth Avenue,
New York, New York,
of Counsel.

IN THE

United States Supreme Court

October Term, 1952

No. 715

ANTHONY WILKO,

Petitioner,

against

JOSEPH E. SWAN, *et al.,*

individually and doing business under the firm name and style of Hayden, Stone & Co.,

Defendants-Respondents,

and

HAVEN B. PAGE,

Defendant.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR PETITIONER TO RESPONDENTS OPPOSITION BRIEF HEREIN

Petitioner submits the following reply to respondent's brief herein.

I.

Contrary to respondent's contentions (see opening paragraph—page 4), the relationship between petitioner and respondents herein was *not* controlled by all the terms and conditions of the margin agreement executed by petitioner dated May 2, 1950 but only by those terms and

conditions which are not in violation of paragraph 2 thereof, which provides that:

> "all transactions made by you (respondent) or your agents for me are to be subject to * * * provisions of the Securities Exchange Act of 1934, and *present* and future Acts amendatory thereof or *supplementary thereto*, and to the Rules and Regulations of the Federal Securities and Exchange Commission * * * *"

The arbitration clause of this agreement is in direct and categorical violation of paragraph 2 of said agreement.

Section 14—(77n) of the Securities Act of 1933 as well as parallel sections of the five other Securities and Exchange Commission statutes provide that:

> "Any condition, stipulation or provision binding any person to waive compliance with *any provisions* of the Act or *any rule of Commission shall be void.*" (Emphasis supplied).

There is nothing ambiguous in this language.

The official policy of the Securities and Exchange Commission has been quite recently (1951) restated and clarified in Securities Act Release No. 3411 of April 10 of that year, from which the following provisions are cited:

> "All the statutes administered by the Commission provide that any condition, stipulation or provision which binds any person to waive compliance with their requirements *shall be void.* Apart from these provisions, moreover, the courts have repeatedly held that a hedge clause or legend disclaiming liability has little, if any, legal effect as protection against civil liability where a person makes a representation which he knows, or in the exercise of reasonable care could have been discovered, is false and misleading. (See cases cited *infra* in "Securities Regulation" by Louis Loss, formerly Associate General Counsel, Securities and Exchange Commission, pages 1074-77).

II.

Respondent's counsel states on page 4, paragraph 3, of his reply brief that:

> "The Court of Appeals noted that petitioner made no claim of 'fraud or coercion' in procuring his signature to the agreement."

Later at the end of page 5, paragraph 3, respondent's counsel says:

> "These constituted the whole record: petitioner submitted no opposing affidavit."

Here are the two fragile and fictitious reeds upon which both the Court of Appeals and Respondents base their case. No customer has any opportunity whatsoever to negotiate any customer's agreement with the respondent herein or any member of the New York Stock Exchange. The customer is handed an agreement already printed like the one herein, and told to sign it as an essential condition precedent to transacting any business whatsoever with the member firm. The only possible negotiations are those between respondent and his counsel in preparing the agreement; the customer's agreement being presumably prepared by respondent's attorneys herein for a fee. The agreement, in both its letter and spirit, was designed to circumvent and nullify the federal securities legislation which the respondent and its co-members of the New York Stock Exchange fought bitterly to defeat for decades, and more particularly up to its enactment the early days of 1933. Respondents are still chafing under federal supervision. The respondent herein is acting in contempt of Securities and Exchange Commission, the very agency which is specifically charged by Acts of Congress, after prolonged consideration and debate, with the regulation of securities transactions on nationally registered exchanges.

The above regulation has been going on for over twenty years.

Respondent's attorneys herein repeatedly harp on the presence of the Bijur affidavit and the absence of any counter-affidavit of petitioner. The Bijur affidavit is the sheerest surplusage and the most general of general denials.

Like margin agreements of the same character signed by customers and member firms, these agreements are not negotiated agreements. Their signing is accomplished by duress on the customer who must sign or take his business elsewhere. These agreements are submitted to customers on printed forms without any arms length bargaining whatsoever. The customer cannot even place his first order to buy or sell before signing such an agreement. The presence or absence of the Bijur affidavit was not considered worthy of any consideration by either Judge Goddard of the District Court or Judge Clark of the Circuit Court, the latter having written the dissenting opinion herein. Respondent's attorneys herein only devote three words to Judge Clark's dissent, to wit: ("Judge Clark dissenting"). See page 5, paragraph 2 therein.

The Bijur affidavit gives no detailed denial of the representations to petitioner at the time his orders for Air Associates stock were executed.(1)

(All the judges herein had before them the printed copies of the customer's agreements herein. That these agreements are signed under definite duress is something which all Judges in the Federal Courts of New York City could have and should have taken judicial notice. Courts in Foley Square are only a few blocks away from the premises of the New York Stock Exchange. It is amazing to find as many as two Judges of the C.C.A. 2nd Circuit committing such an egregious error.)

---

(1) Petitioner has executed and would, with the permission of this Court, submit a counter-affidavit, setting forth the duress to which he was at that time subjected.

III.

The instant case is in exactly the same position as was the *Shanferoth Case* where the petitioner applied for a writ of certiorari which the Supreme Court granted.(1)

It is highly significant to note that respondent cited the Shanferoth case copiously in order to have his appeal to the Circuit Court of Appeals. Once respondent gets a favorable decision in the C.C.A. he does not wish the appeal to go further. It should be noted that respondent does not mention the Shanferoth case at all in his opposition brief to petitioner's application for the writ of certiorari herein.

It is quite obvious that should respondent by any chance block the application of petitioner herein, he would plead res judicata immediately and invoke the *Shanferoth Case* to enforce compulsory arbitration.

Consequently the instant case is specifically and definitely ripe for review at this moment.

IV.

Both the majority of the Circuit Court and respondent's attorneys herein err in concluding that "the arbitrators are bound to decide in accordance with the provisions of Section 12 (2) "of the Securities Act of 1933". Of what use is it to have arbitrators bound to decide in accordance with federal statutes when such arbitrators, with few exceptions, have neither the professional training or experience to enable them to understand all the provisions of the Securities and Exchange Commission statutes and their rules and regulations, not to mention the laws of evidence?

---

(1) 293 U.S. 449.

V.

Later on page 6 of their reply brief respondents conjure up the spectre of *speculative fears* and the dangers of premature review of interlocutory proceedings. There are no speculative fears herein.

Congress had in mind real fears when they enacted the Securities Act of 1933 and which the Securities and Exchange Commission itself still has in mind. Respondents conjure up red herrings and bogey men in an effort to intimidate the United States Supreme Court and the petitioner. These chimaera were not thought worthy of mention by either Judge Goddard or Judge Clark (dissenting) herein. The real—not speculative fears herein, are those of the respondents who are afraid to face any jury trial in their own jurisdiction.

Respondents have no witness to support their case herein. The customer's representative of Hayden Stone & Co., who handled the Wilko account has died since the commencement of this action, so petitioner's attorney is informed. The facts to be developed are extremely simple.

VI.

Distrust of arbitration is neither ancient or supposedly outmoded. The Supreme Court has repeatedly held that there are certain types of controversies that should not be settled by arbitration.(1) The instant case is one of these controversies. This Court is again referred to the following section of Judge Clark's dissenting opinion on page 52 of the transcript of the record:

> "The role of the burden of proof concept is to canalize and control the evidence; it may often be the decisive factor in the case. . . . the arbitrators will act according to their business background and there will

(1). See Judge Goddard's opinion herein; also 165 Fed (2) 746 and 58 U.S. 344.

be no way of checking what they do. . . So what is most desirable in the ordinary arbitration becomes the clear loss of a statutory right here."

Respondent again cites affirmatively the case of *Donahue* v. *Susquehanna Collieries Co.*, 138 Fed. 2d 3, 6 (3d Cir. 1943). Petitioner has already called attention to the fact that this case was litigated as a result of a transaction *in coal* and not *in securities*, and from legislation pre-dating the Securities Act of 1933.

VII.

The balance of Respondent's brief in opposition herein is full of errors and sophistries. Petitioner has never said that the purchaser must sue in every case of a dispute with a member of the New York Stock Exchange. What petitioner has said is that the purchaser must not be required to submit to arbitration if he prefers to avail himself of his statutory rights to seek relief in the courts which are paramount to any agreement to arbitrate.

Respondents ignore the fact completely that there are only two fora where an arbitration can be handled in the jurisdiction of the Southern District of New York (1) The New York Stock Exchange and (2) the American Arbitration Association. Arbitrators are not special masters or officers of the Court.

Respondents have completely ignored the House of Representatives' report of their hearing prior to the adoption of the Federal Arbitration Act of 1924, which stated that: when the arbitration machinery has been undertaken

> "The arbitration proceeds without interference by the Court. The award may then be entered by a judgment, subject to attack by the other party for fraud and corruption and similar undue influence, or for palpable error in form".

See H. Rep. No. 96, 68th Congress, 1st Session (1924) page 2.

VIII.

Respondent's references on page 13 as to English arbitrations have no relevancy herein. Respondents are still living in the day of George III, and not after the adoption of the Constitution of the United States and the enactment of the Securities Act of 1933. Similarly the arbitrations in the New York courts have no relevancy in this proceeding which is in the United States Courts.

In the second paragraph on page 14 of Respondents' reply brief herein, their counsel attempt to throw another smoke-screen around petitioner and amicus curiae herein. The contractual agreement herein does not benefit petitioner. It penalizes him in the transaction of business with respondent. Respondents' agreement makes it clear that such agreement is drawn for the benefit and exculpation of the respondent and at the expense of the petitioner.

Respondents fear arbitration, otherwise they would not make such desperate and far fetched efforts to enforce it. Respondents are challenged to rewrite their customer's agreement herein, and put the compulsory arbitration clause at the beginning of the contract, and the clause stating their devotion to the jurisdiction of the Securities and Exchange Commission at the bottom of the agreement just above the place for the customer's signature.

IX.

The growing importance of this case is shown by the comment under recent cases in the recently published (May 1953) Volume 66, Number 7, page 1326 of the Harvard Law Review in which the Editor states that "arbitration seems an improper method for resolving the issue in the instant case." et sequitur

For the above reasons, the writ of certiorari asked for by the petitioner should be granted.

HENRY E. MILLS,
20 Pine Street,
New York, New York,
Attorney for Petitioner.

RICHARD H. WELS,
551 Fifth Avenue,
New York, New York,
of Counsel.

LIBRARY
SUPREME COURT. U.S.

Office - Supreme Court, U. S.
FILED
OCT 14 1953
HAROLD B. WILLEY, Clerk

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1953

No. 39

ANTHONY WILKO,

Petitioner,

vs.

JOSEPH E. SWAN, ET AL., INDIVIDUALLY AND DOING BUSINESS UNDER THE FIRM NAME AND STYLE OF HAYDEN STONE & CO., AND HAVEN B. PAGE

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITIONER'S BRIEF

HENRY E. MILLS,
Counsel for Petitioner.

RICHARD H. WELS,
Of Counsel.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1953

No. 39

ANTHONY WILKO,

Petitioner,

vs.

JOSEPH E. SWAN, ET AL., INDIVIDUALLY AND DOING BUSINESS UNDER THE FIRM NAME AND STYLE OF HAYDEN, STONE & CO., AND HAVEN B. PAGE

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITIONER'S BRIEF

POINT I

Compulsory Arbitration Clauses in the Customer's Agreements Signed by the Petitioner and the Respondent Are Void under the Non-Waiver Provisions of the Securities Act of 1933. The Federal Arbitration Act of 1925 Is Inapplicable Because of the Overriding Provisions of the Securities Act of 1933.

The principal question herein is whether the provisions of the Federal Arbitration Act of 1925 require controversies

between the parties herein to be settled by arbitration, or whether such agreement is specifically voided by the express provisions of the Securities Act of 1933, even if the parties herein have so agreed in writing.

Prior to the enactment of the Federal Arbitration Act, arbitration was unenforceable in the Federal Courts. The purpose of that Act was to *permit*, not to require arbitrations in certain controversies, subject to limited review in the Federal Courts.

The Securities Act of 1933 was enacted subsequently to the Arbitration Act of 1925 and resulted from extensive Congressional investigations into the investment banking and securities fields. The Securities Act evidenced a strong Congressional purpose to afford the purchaser of securities adequate protection against the seller. Congress recognized that the investor must be given adequate weapons in the civil courts, and to this end, shifted the burden of proof from the plaintiff to the defendant in civil actions, and in effect changed the principle of "caveat emptor" to "caveat venditor".

The Securities Act of 1933 provided further that any waiver by the purchaser of securities of his rights under the Securities Act was void.[1] It is significant that Congress used the word "void", and not the word "voidable", which should dispel any notion that this section of the statute is merely mandatory.

The Securities Act of 1933 clearly expressed the purposes of Congress, and more particularly demonstrated conclusively that its non-waiver provisions over-ride any conflicting provisions of the Federal Arbitration Act of 1925.

These arguments have been comprehensively briefed by the Securities & Exchange Commission, which, with the permission of the courts, herein, has appeared as amicus

[1] See U.S.C.A. Title 15, Chapter 2a, Sections 77K and 77L.

curiae. Petitioner herein can add little to what has already been argued so effectively by the Commission. To avoid unnecessary repetition petitioner accordingly adopts and relies upon the arguments presented by the Commission to the Federal Courts upon this point.

Point II

Even if the Federal Arbitration Act of 1925 Were Applicable in Certain Cases, the Compulsory Arbitration Clause of the Customer's Agreement Could Not Be Invoked in the Case at Bar.

The Federal Arbitration Act of 1925 provides that arbitration agreements cannot be enforced if there are grounds in law or in equity for the revocation of the contract.[2]

The agreement of the parties herein provides that any provision "shall be deemed modified or superseded"[3] by any statute which is in any manner inconsistent with such provision. The arbitration clause in the agreement refers to "any controversy between us under this contract."

The above agreement was signed just prior to the opening of the petitioner's account with the respondent, and Petitioner purchased securities on the basis of fraudulent representations made by the respondent. Such representations necessarily affected all of the terms and provisions of the customer's agreement. In the absence of any denial by the respondent of the making of fraudulent representations, they must be assumed to have been made, and grounds at law or in equity for the revocation of the agreement must have necessarily existed. Hence the Federal Arbitration Act of 1925 by virtue of its own provisions must be inapplicable.

---

[2] See U.S. Code Annotated, Title 9, Section 10.

[3] See Customer's Agreement herein.

The Customer's agreement herein contains many provisions as to the respective rights and liabilities of the parties, including an exculpatory clause favoring respondents, which the Court of Appeals for the 2d Circuit has already found to be void and illegal. Many respondents and other brokerage houses insist that an agreement be signed before the customer may open an account and commence dealing in securities. These conditions amount to duress as a matter of law (3a—3b):

3a—Probably the most comprehensive as well as the most recent discussion of the subject of non-waiver provisions of the civil liabilities of the SEC statutes generally is to be found on pages 1074-1077 of "SECURITIES REGULATION" by Louis Loss, published by Little Brown & Co. in the latter part of 1951[4] From page 1075 of the above volume we quote as follows:

> "All six SEC statutes specify that any condition, stipulation or provision binding any person to waive compliance with any provision of the act or any rule of the Commission '*shall be void.*'"

3b—Further on page 1076 of "SECURITIES REGULATION" appears the following:

> "In a recent (1951) opinion of the General Counsel, he ruled that 'the anti-fraud provisions of the SEC statutes are violated by the employment of any legend, hedge clause or other provision, which is likely to lead any investor to believe that he has in any way, waived any action he may have.'"

---

[4] Louis Loss is the former Associate General Counsel of the Securities & Exchange Commission, and is presently on the faculty of the Harvard Law School.

Point III

United States District Courts Have No Right To Supervise the Conduct of an Arbitration Proceeding

The majority of the bench in the Circuit Court of Appeals herein was obviously troubled by the fact that the Securities Act of 1933 shifts the burden of proof from the purchaser to the seller of securities, and was aware that arbitrators are not required to observe the rules of evidence or rules of proof. It met this uncomfortable situation by suggesting that, if the arbitrators failed to comply with the requirements of the Securities Act of 1933, the District Court could, by invoking its "powers" to supervise the arbitration, set aside the award of the arbitrators herein.

The Federal Arbitration Act of 1925 confers no authority upon federal courts to supervise the conduct of an arbitration. Nor does any other statute. On the contrary, the arbitration agreement signed by the parties herein and the Courts (including this court) have held that the award of the arbitrators is final, and may not be reviewed, except in certain situations involving corruption, partiality and similar misbehavior on the part of the arbitrators. ([5]) ([6])

Summary of Argument

Petitioner maintains:

1. The compulsory arbitration provisions of the customer's agreement signed by the petitioner and the respondent are void under the non-waiver provisions of the Securities Act of 1933.[7]

---

[5] U.S.C.A. Title 9, Section 10, including in particular *Shanferoke Coal and Supply Corporation* vs. *Westchester Service Corp.*, 70 Fed. 2,297 and 293 U.S. 449.

[6] *American Almond Products Co.* vs. *Consolidated Pecan Sales Co., Inc.*, 144 Fed. 2d 448 et seq.—C.C.A. 2d Circuit 1944.

[7] 15 U.S. Code Annotated Sections 77L and 77N.

2. Even if the Federal Arbitration Act of 1925 was generally applicable, the compulsory arbitration provisions of the customer's agreement herein, could not be invoked in the case at bar.[8]

3. The United States District Courts have no authority to supervise the conduct of an arbitration proceeding involving securities transactions in violation of the express provisions of the Securities Act of 1933, as well as other Acts amendatory and supplementary thereto.

HENRY E. MILLS,
Attorney for Petitioner,
20 Pine Street,
New York, N. Y.

RICHARD H. WELS,
Of Counsel,
551 Fifth Avenue,
New York, N. Y.

[8] 9 U.S. Code Annotated.

INDEX

	Page
Opinions below	1
Jurisdiction	2
Question presented	2
Statutes involved	3
Statement	6
Specification of error to be urged	9
Reasons for granting the writ	9
Conclusion	21

CITATIONS

Cases:

Agostini Bros. Building Corp. v. *United States*, 142 F. 2d 854	16
American Almond Products Co. v. *Consolidated Pecan Sales Co., Inc.*, 144 F. 2d 448	18, 20, 21
The Anaconda v. *American Sugar Refining Co.*, 322 U. S. 42	16
Boyd v. *Grand Trunk Western R. Co.*, 338 U. S. 263	13, 17
Burchell v. *Marsh*, 58 U.S. 344	21
Callen v. *Penna. R. R.*, 332 U. S. 625	17
Canadian Gulf Line, Ltd., In re, 98 F. 2d 711	20
Donahue v. *Susquehanna Collieries Co.*, 138 F. 2d 3	16
Donahue v. *Susquehanna Collieries Co.*, 160 F. 2d 661	20
Evans v. *Hudson Coal Co.*, 165 F. 2d 970	19
Hill v. *Hill*, 199 Misc. 1035, 104 N. Y. S. 2d 755	16
Jefferson Lake Sulphur Co. v. *Walet*, 104 F. Supp. 20, affirmed, *Walet* v. *Jefferson Lake Sulphur Co.*, C. A. 5, March 11, 1953, CCH Fed. Sec. L. Rep. ¶ 90,616	15
Karppinen v. *Kari Kiefer Machine Co.*, 187 F. 2d 32	20
Kingswood Management Corp. v. *Salzman*, 272 App. Div. 328, 70 N. Y. S. 2d 592	16
Murphy v. *Cady*, 30 F. Supp. 466, affirmed, 113 F. 2d 988, certiorari denied, 311 U. S. 705	12
James Richardson & Sons, Ltd. v. *W. R. Hedger Trans. Corp.*, 98 F. 2d 55, certiorari denied, 305 U. S. 657	20
S.E.C. v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344	15
Swislocki v. *Spiewak*, 273 App. Div. 70[illegible], 75 N. Y. S. 2d 147	16
United Fuel Gas Co. v. *Columbian Fuel Corp.*, 165 F. 2d 746	20
Watkins v. *Hudson Coal Co.*, 151 F. 2d 311, certiorari denied, 327 U.S. 777	16
Zip Mfg. Co. v. *Pep Mfg. Co.*, 44 F. 2d 184	16

Statutes:

Page

Securities Act of 1933:

Section 11, 15 U. S. C. 77k 10
Section 12(2), 15 U.S.C. 77l(2) 2, 3, 9, 11, 12, 13, 19, 20
Section 14, 15 U. S. C. 77n 2, 3, 13, 14, 15
Section 16, 15 U. S. C. 77p 11
Section 22(a), 15 U. S. C. 77v(a) 4, 13

Securities Exchange Act of 1934:

Section 16(b), 15 U. S. C. 78p(b) 15
Section 29(a), 15 U. S. C. 78cc(a) 15

Federal Arbitration Act:

Section 3, 9 U. S. C. 3 4
Section 10, 9 U. S. C. 10 ..... 2, 5, 19

Legislative History:

H. Rep. No. 85, 73d Cong., 1st Sess. 11, 12, 14
S. Rep. No. 47, 73d Cong., 1st Sess., pp. 6-7 12

Miscellaneous:

American Arbitration Association, Commercial Arbitration Rules, Rule 30 19
Chamber of Commerce of the State of New York, *Handbook and Guide to Arbitration under the New York and United States Arbitration Statutes* (1932), pp. 4-6 18
Loss, *Securities Regulation* (1951), pp. 1011-1029 12

New York Stock Exchange:

Constitution, Art. VIII, Sec. 4, 6 18
Rules of the Board of Governors, Rule 754 18

In the Supreme Court of the United States

OCTOBER TERM, 1952

No. 715

ANTHONY WILKO, PETITIONER

v.

JOSEPH E. SWAN, ET AL., INDIVIDUALLY AND DOING BUSINESS UNDER THE FIRM NAME AND STYLE OF HAYDEN STONE AND CO., ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR SECURITIES AND EXCHANGE COMMISSION, AMICUS CURIAE, IN SUPPORT OF PETITION

The Solicitor General submits this brief on behalf of the Securities and Exchange Commission, *amicus curiae*, in support of the petition for a writ of certiorari.

OPINIONS BELOW

The opinion of the Court of Appeals (R. 40-49) is reported in 201 F. 2d 439. The opinion of the District Court (R. 23-32) is reported in 107 F. Supp. 75.

JURISDICTION

The judgment of the Court of Appeals was entered on January 15, 1953 (R. 52). The petition for a writ of certiorari was filed on April 14, 1953. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254. See also Section 22(a) of the Securities Act of 1933, 15 U.S.C. § 77v(a).

QUESTION PRESENTED

Whether an agreement to arbitrate a cause of action arising under the civil liabilities provisions of Section 12(2) of the Securities Act of 1933, obtained by a securities firm from a customer at the initiation of their dealings, is valid and enforceable in view of the purpose of Congress to make available to a defrauded purchaser of securities the simple and effective court remedy provided by Section 12(2) encompassing litigation advantages which may not be afforded or safeguarded in an arbitration proceeding, and in view of the provisions of Section 14 of said Act invalidating agreements to waive compliance with the statute.[1]

---

[1] The determination below also presents the question whether the provisions of the Federal Arbitration Act for vacating an award (9 U.S.C. § 10) authorize a court to compel compliance with an arbitration agreement which (as construed by the court below) requires that the arbitrators abandon their normal functions and conduct the equivalent of a court proceeding. The Commission, however, has no distinct statutory interest in the proper construction of the Federal Arbitration Act, and discusses this question only to the extent that it is pertinent to the principal question set forth in the text.

STATUTES INVOLVED

The following are the pertinent provisions of the Securities Act of 1933:

Section 12(2), 15 U.S.C. § 771(2):

> Any person who—
>
> * * * * *
>
> (2) sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission, shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

Section 14, 15 U.S.C. § 77n:

> Any condition, stipulation, or provision binding any person acquiring any security to

waive compliance with any provision of this title or of the rules and regulations of the Commission shall be void.

Section 22(a), 15 U.S.C. § 77v(a):

The district courts of the United States, the United States courts of any Territory, and the Supreme Court of the District of Columbia shall have jurisdiction of offenses and violations under this title and under the rules and regulations promulgated by the Commission in respect thereto, and, concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this title. Any such suit or action may be brought in the district wherein the defendant is found or is an inhabitant or transacts business, or in the district where the sale took place, if the defendant participated therein, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 128 and 240 of the Judicial Code, as amended (U.S.C., title 28, secs. 225 and 347). No case arising under this title and brought in any State court of competent jurisdiction shall be removed to any court of the United States. * * *

The Federal Arbitration Act provides:

9 U.S.C. § 3:

If any suit or proceeding be brought in any of the courts of the United States upon

any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

9 U.S.C. § 10:

In either of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration—

(a) Where the award was procured by corruption, fraud, or undue means.

(b) Where there was evident partiality or corruption in the arbitrators, or either of them.

(c) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced.

(d) Where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

* * * * *

STATEMENT

Petitioner charged in his complaint that, on or about January 17, 1951, respondents sold him 1,600 shares of the common stock of Air Associates, Inc., for $29,517.24, by means of misrepresentations of material facts and omissions to state material facts necessary to make various representations not misleading. Respondents are the partners of Hayden, Stone & Co., a New York securities firm. Haven B. Page, a director and counsel of Air Associates and whose stock allegedly was sold, is also a defendant. Claiming to have suffered a loss of $3,888.88 as a result of respondents' misrepresentations when he sold the stock two weeks later, petitioner brought this action under the civil liabilities provisions of Section 12(2) of the Securities Act of 1933 to recover that amount. (R. 2-4.)

Without answering the complaint, respondent Hayden, Stone & Co. moved for a stay pursuant to the Federal Arbitration Act, 9 U.S.C. § 3, and submitted an affidavit which disclosed that on May 2, 1950, apparently in connection with an earlier unrelated transaction, and again on January 18, 1951, in connection with the instant sale, petitioner had signed a form "Margin Agreement" which this firm used in its dealings with its customers (R. 7-10). The form agreement is reproduced in larger type in six pages of the Transcript of the Record (pp. 11-16); but the document attached to the affidavit was a fine print form, approximately 8½ by 11 inches, containing on one side of the page numerous provisions respecting the rights and liabilities of the parties.

The seventeenth paragraph of this printed form contains the following provision for arbitration (R. 16, 22):

> Any controversy arising between us under this contract shall be determined by arbitration pursuant to the Arbitration Law of the State of New York, and under the rules of either the Arbitration Committee of the Chamber of Commerce of the State of New York, or of the American Arbitration Association, or of the Arbitration Committee of the New York Stock Exchange or such other Exchange as may have jurisdiction over the matter in dispute, as I may elect. Any arbitration hereunder shall be before at least three arbitrators.

Among the other provisions is one (apparently dealing with business and technical questions) which states that all transactions effected on the customer's behalf are subject to the constitutions, rules, customs and practices of the exchanges or markets where executed and of their respective clearing houses, and to "the provisions of the Securities Exchange Act of 1934 and present and future acts amendatory thereof or supplemental thereto", and to applicable rules and regulations of the Securities and Exchange Commission (R. 11, 17).

Elsewhere in the form agreement is a paragraph in which respondents purportedly are exculpated from liability for any misrepresentations made by them, or by their agents or employees, in the sale or purchase of securities (R. 14, 20).

The contract for the sale of the stock was a separate agreement (R. 26).

District Judge Goddard denied respondents' motion for a stay pending arbitration. The arbitration agreement obtained by respondents "as a preliminary to the purchase of stock," he ruled, conflicted with the Securities Act of 1933 in attempting to deprive petitioner of the advantageous court remedy which Congress intended to afford a defrauded purchaser under Section 12(2) of that Act. Moreover, he held, it amounted to a waiver of compliance with the statute and was therefore rendered void by Section 14 of the Act. (R. 23-32.)

A divided Court of Appeals reversed the order of the District Court (R. 40-52). The majority of the court (Judges Swan and Chase), although observing that the "question is not free from doubt" (R. 49), ultimately concluded that the Securities Act of 1933 did not prohibit a securities firm from obtaining a pre-sale or pre-controversy agreement for the arbitration of any cause of action, including the statutory action for fraud or misrepresentation which a customer may later have reason to assert. The majority held, accordingly, that the stay provisions of the Federal Arbitration Act (9 U.S.C. § 3) were applicable (R. 41-49).

Judge Clark wrote a dissenting opinion in which he expressed the view that, under the ruling of the majority, "important rights under this notable first of a series of famous Acts for the benefit of the investing public [would] be capable of nullifica-

tion by long fine-print restrictions of the broker's devising" (R. 52).

The Securities and Exchange Commission participated as *amicus curiae* in the proceedings in both courts below in opposition to the motion to stay the court action and compel arbitration.

SPECIFICATION OF ERROR TO BE URGED

While petitioner has assigned a sizeable list of errors, the interest of the Commission as *amicus curiae* extends only to the following:

The majority of the Court of Appeals erred in holding that the pre-sale agreement for compulsory arbitration is valid and enforceable against the petitioner customer in a subsequent action for fraud in the sale of securities brought against the respondent securities firm pursuant to Section 12(2) of the Securities Act of 1933.

REASONS FOR GRANTING THE WRIT

I

Upon what it regarded as a close question of statutory construction—and one of great importance to the investing public—the majority below reached a decision which opens the door to nullification of important rights under the Securities Act of 1933 which Congress intended to afford public investors. The question is whether the Securities Act of 1933 permits a securities firm to resort to a pre-sale or pre-controversy arbitration agreement in order to avoid court actions under the civil liabilities provisions of that statute which may be in-

stituted by customers who believe that they have been defrauded. We show below that arbitration cannot assure the customer the equivalent of his statutory rights. As Judge Clark aptly observed in his dissent, the majority of the Court of Appeals ignored the realities of the relationship between the professional securities firm and the ordinary customer in holding that the petitioner customer had effectively waived his statutory choice of remedies by executing the form agreement prior to the transaction which gave rise to his asserted cause of action. While the stipulation here in question was exacted by a broker-dealer in connection with the opening of an account, the decision below may well suggest exaction of similar stipulations for arbitration by issuers and underwriters who desire to avoid lawsuits under the companion civil liabilities provisions of Section 11 of the Act, 15 U.S.C. § 77k, on account of misrepresentations or omissions in registration statements.

The majority below described the opinion of the District Court as "carefully reasoned" (R. 43), and one which "presents a strong argument against the conclusion we have reached" (R. 49). It agreed also that the Commission's *amicus curiae* brief had made a "strong presentation" in support of the decision of the District Judge (R. 43). Conceding that "the question is not free from doubt" (R. 49), it determined nevertheless, to resolve that doubt against the interests of the investing public which the Securities Act of 1933 was designed to protect. The minority opinion of

Judge Clark expressed high regard for commercial arbitration as a method of "bringing a businessman's adjudication to business questions" (R. 49-50). "But", Judge Clark cautioned, "it would be vastly unfortunate if it became usable as a device to blunt or break social legislation" (R. 50). In his view, the majority has sanctioned such a device; and his opinion sets forth reasons why "what is most desirable in the ordinary arbitration becomes a clear loss of statutory right here" (R. 51). Unless reversed by this Court, the ruling will be *stare decisis* in the circuit containing the nation's largest financial community and the hub of the country's securities industry. Review by this Court, we suggest, is clearly desirable in the public interest.

II

In enacting Section 12(2) and the other civil liabilities provisions of the Securities Act of 1933, Congress intended to afford defrauded customers litigation advantages which were necessary for their protection but which were not considered unfair to the securities industry. The heavy burden imposed upon a plaintiff in a common law action for fraud and deceit arising out of a securities transaction convinced Congress that a simpler and more effective court remedy was needed.[2] Section 12(2) is part of a statutory scheme which resulted from the conclusion of Congress that securities are "intricate merchandise",[3] and that the public in-

[2] The common law remedies, however, were preserved by Section 16 of the Act, 15 U.S.C. § 77p.

[3] H. Rep. No. 85, 73d Cong., 1st Sess. (1933), p. 8.

terest demanded legislation which would recognize the gross inequality of bargaining power between the professionals in the securities business and the average investor. The Act was passed in response to a Presidential message urging that there be added to the ancient rule of *caveat emptor* the further doctrine "let the seller also beware",[4] and the reports of the congressional committees recognize this important goal.[5]

Under Section 12(2), the burden of proof is shifted to the defendant seller who must prove "that he did not know, and in the exercise of reasonable care could not have known, of [the] untruth or omission." The legislative history discloses that Congress recognized that, as a practical matter, if more than mere "paper liability" was to be imposed upon fraudulent vendors of securities, "it is necessary to throw the burden of disproving responsibility for reprehensible acts of omission or commission" on the seller. "To impose a lesser responsibility", it was felt, "would nullify the purposes of this legislation." H. Rep. No. 85, 73d Cong., 1st Sess. (1933), pp. 9-10. In 1934, when Congress enacted some alleviating amendments with respect to Section 11, it left Section 12(2) untouched.[6]

---

[4] *Id.*, at 2.

[5] *Ibid.*; S. Rep. No. 47, 73d Cong., 1st Sess. (1933), pp. 6-7.

[6] For a detailed discussion, see Loss, *Securities Regulation* (1951), pp. 1011-1029. The advantage of the Section 12(2) remedy over the common law action for fraud and deceit is illustrated by *Murphy* v. *Cady*, 30 F. Supp. 466 (D. Maine), affirmed, 113 F. 2d 988 (C.A. 1), certiorari denied, 311 U.S. 705, where the court dismissed the common law count of the complaint but sustained the statutory action on the same allegations of fact.

The statute also affords the defrauded purchaser a broad choice of forum. He may sue in any court of competent jurisdiction—federal or state. If he sues in a state court, the action cannot be removed to a federal court; and if he elects to sue in a federal court he has a broad choice of venue, with the privilege of nation-wide service of process, and he need not comply with the $3,000.00 requirement of diversity cases. See Section 22(a).[7]

That Congress intended this civil remedy to be always available to a customer who finds that he has been defrauded is made clear by the aforementioned legislative history, and by the anti-waiver provisions of Section 14 of the Act. The latter expressly state that any "stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this title * * * shall be void." The decision below gives effect to a stipulation, exacted at the very initiation of the customer's dealings with the securities firm, pursuant to which the customer waives his right, in the event of a fraudulent sale, to elect the remedy provided by Section 12(2) and the consequent choice of forum and shift in the burden of proof. In our opinion, this involves to a very material degree a waiver of "compliance" with the statute.

---

[7] *Cf. Boyd* v. *Grand Trunk Western R. Co.*, 338 U. S. 263, 266, where the Court regarded the choice of venue granted by Section 6 of the Federal Employers' Liability Act as so "substantial" that a stipulation restricting that choice was held invalid as a "device" which "would thwart the express purpose of the Federal Employers' Liability Act."

The majority below, however, found it "far from clear that the words 'waive compliance with' refer to anything more than the mandatory or prohibitive provisions of the Act." It observed: "The means of enforcement provisions, on the other hand, seem clearly permissive, not requiring compliance" (R. 47). Section 14, of course, refers to "any provision of" the Act. To construe the section as voiding only attempted waivers of compliance with the substantive provisions of the Act, such as the prohibitions against fraud and misrepresentation, rather than the remedial provisions, runs counter to the purpose of the statute. Moreover, to the extent that enforcement of the substantive requirements of the Act is dependent upon the effectiveness of the private remedies afforded, the view of the majority below can only tend to undermine compliance with the substantive provisions as well. See H. Rep. No. 85, 73d Cong., 1st Sess. (1933), pp. 9-10, *supra*, p. 12. Thus, if an investor, in advance of his dealings with a securities firm, may be induced to contract away all of his remedial rights under the Act, the obvious consequence is to render nugatory those remedies and to make compliance with the substantive provisions dependent exclusively upon the criminal and injunctive sanctions. The opinion of the Court of Appeals does not go that far; for the waiver of compliance permitted below contemplated the substituted remedy of arbitration. If, however, the language "waive compliance with any provision of this title" is not construed to cover waiver of the statutory remedies, there appears no

logical stopping place short of complete evisceration of those remedies.

On the other hand, if the quoted language does cover remedies, we believe that it necessarily preserves all of the public investor's remedies under the statute, and forbids any of them to be bargained away in advance of the transaction giving rise to the customer's claim. In that respect it is immaterial whether the consideration for the waiver be the substituted procedure of arbitration, a stipulation for liquidated damages of a lesser amount than that provided by the statute, or something else. The majority below suggested that Congress would have included a specific prohibition against arbitration in Section 14 had it intended that provision to have such broad coverage. Congress has seen fit, however, to cover the matter of waivers by a single broadly worded prohibition rather than by particularization of specific types of waivers. *Cf. Jefferson Lake Sulphur Co.* v. *Walet*, 104 F. Supp. 20 (E.D. La.), affirmed, *Walet* v. *Jefferson Lake Sulphur Co.*, C.A. 5, March 11, 1953, CCH Fed. Sec. L. Rep. ¶ 90,616.[8] See also *S.E.C.* v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344, 350.

The majority concluded that its interpretation involved no conflict with the policy or purpose of

[8] The same anti-waiver language in Section 29(a) of the companion Securities Exchange Act of 1934, 15 U.S.C. § 78cc(a), was held in that case to make it "crystal clear" that any waiver of the right of a corporation to maintain an action under Section 16(b) of that statute, 15 U.S.C. § 78p(b), to recover the "short" term" trading profits of a corporate insider, would be void (104 F. Supp., at 23-24).

the Securities Act of 1933 (R. 46-49).[9] Assuming it to be conceded that the customer could enter into a binding stipulation to arbitrate or settle his claim out of court after a cause of action arose, it held that a pre-sale or pre-controversy stipulation presented no different question. However, since the Act accords the defrauded customer an election between his statutory and common law remedies, and gives him also a choice of forum, it is arguable that it would not be inconsistent with the purpose of the statute if the customer were permitted to elect to have an existing claim for violation of his substantive rights determined by arbitration rather than by court action. The Commission took no position on this question in the court below and we take none here. We suggest only that if post-con-

---

[9] Apart from the express anti-waiver provisions of Section 14, conflicting public policy, whether determined by the court or the legislature, is sufficient in itself to invalidate an arbitration agreement. See, *e.g.*, *The Anaconda* v. *American Sugar Refining Co.*, 322 U.S. 42, 46 ("* * * a party cannot stipulate away * * * jurisdiction which the legislation declares open * * *."); *Kingswood Management Corp.* v. *Salsman*, 272 App. Div. 328, 70 N.Y.S. 2d 692, 693 ("The Emergency Price Control Act was adopted from urgent reasons of public policy which the Congress did not intend to turn over to private arbitrators to administer"). See also *Zip Mfg. Co.* v. *Pep Mfg. Co.*, 44 F. 2d 184 (D. Del.); *Hill* v. *Hill*, 199 Misc. 1035, 104 N.Y.S. 2d 755 (Sup. Ct.); *Swislocki* v. *Spiewak*, 273 App. Div. 768, 75 N.Y.S. 2d 147.

Of course, the fact that the cause of action asserted may be statutory in origin does not necessarily mean that public policy forbids arbitration. Agreements to arbitrate actions under the Miller Act and Fair Labor Standards Act of 1938, for example, have been regarded as presenting no conflict with the policies of those statutes. See *Agostini Bros. Building Corp.* v. *United States*, 142 F. 2d 854 (C.A. 4); *Watkins* v. *Hudson Coal Co.*, 151 F. 2d 311 (C.A. 3), certiorari denied, 327 U. S. 777; *Donahue* v. *Susquehanna Collieries Co.*, 138 F. 2d 3 (C.A. 3).

troversy agreements to arbitrate are valid, they fall into the category of other post-controversy arrangements which may limit plaintiff's course of action, such as the decision to waive a jury trial, or perhaps to accept a compromise settlement of the claim. We submit that the court below erred in assuming that there can be no substantial distinction between a pre-controversy and a post-controversy stipulation to waive compliance with the remedial provisions of the statute. The grant of latitude for reasonable post-controversy agreements may very well be consistent with the realistic effectuation of the purpose of Congress to afford the investor a choice of remedies.

On the other hand, to uphold the pre-controversy stipulation enables the professional in the securities business to strip the investor of the protection of the statute. Contrary to the purpose of Congress, the decision below has given no recognition to the grossly unequal positions of the securities firm and the average customer who, before effecting a purchase, is requested to sign a fine-print form agreement. A persuasive analogy on this point is mentioned in Judge Clark's minority opinion—*viz.*, the decisions of this Court which give no validity, under the Federal Employers' Liability Act, to releases obtained prior to an accident, but recognize them if fairly and reasonably made in settlement of an existing claim (R. 52).[10] As Judge Clark noted, however, the

[10] See, *e.g.*, *Callen* v. *Penna. R. R.*, 332 U. S. 625, 631; *Boyd* v. *Grand Trunk Western R. Co.*, 338 U. S. 263, 266.

validity of a post-controversy stipulation is not now before the Court.

District Judge Goddard and Circuit Judge Clark correctly pointed out that arbitration could not assure a customer the equivalent of his statutory rights. As Judge Learned Hand has stated, in arbitration the parties "must content themselves with looser approximations to the enforcement of their rights than those that the law accords them, when they resort to its machinery."[11] Commercial arbitration is designed to obtain a businessman's decision of a business question. The arbitrators would be selected by the regulated industry,[12] and would ordinarily be laymen who would hear and decide the claim without reference to technical rules of law and procedure.[13] There is no assurance that the arbitrators would or could correctly apply the rules of procedure, the principles of evidence, the substantive law of fraud and misrepresentation, the statutory burden of proof, and the correct measure of damages. There is no assurance, moreover, that lay arbitrators would not be influenced in some degree by the exculpatory provision of the margin agreement which is concededly invalid. Finally, as the dissenting judge observed, it is improbable

---

[11] *American Almond Products Co.* v. *Consolidated Pecan Sales Co., Inc.*, 144 F. 2d 448, 451 (C.A. 2).

[12] See, *e.g.*, Art. VIII, Sections 4 and 6, of the Constitution, and Rule 754 of the Rules of the Board of Governors of the New York Stock Exchange.

[13] See *Handbook and Guide to Arbitration under the New York and United States Arbitration Statutes*, issued by the Chamber of Commerce of the State of New York (1932), pp. 4-6.

that industry arbitrators would give "the customer that objective and sympathetic consideration of his claim which is envisaged by the Securities Act" (R. 50).

III

The majority of the Court of Appeals was not unconcerned with these dangers. It felt, however, that they would be avoided in this case because (1) it construed the margin agreement to require, by implication, that the arbitrators apply the provisions of the Securities Act of 1933, and (2) it considered that, therefore, a decision by the arbitrators not reached in conformity with Section 12(2) could be vacated by the court under Section 10 of the Federal Arbitration Act, 9 U.S.C. § 10. The majority, however, gave no consideration to the various arbitration associations' rules expressly adopted by the margin agreement with which a simulated court trial would appear to conflict.[14]

While we assume that an award which expressly relied upon the invalid exculpatory clause in the margin agreement could be set aside,[15] the pos-

[14] Thus, the rules of the American Arbitration Association provide that "the arbitrator shall be the judge of the relevancy and materiality of the evidence offered and conformity to legal rules of evidence shall not be necessary." Rule 30 of the Commercial Arbitration Rules.

[15] *Cf. Evans* v. *Hudson Coal Co.*, 165 F. 2d 970 (C.A. 3), where the court prescribed a wage formula for the guidance of the arbitrators so that their award might not later be set aside as based upon a formula rendered illegal by the Fair Labor Standards Act. The requirement that arbitrators make mathematical computations in conformity with such formula, of course, falls within the normal functions of lay arbitrators.

sibility of judicial review of an award does not permit the court to exercise supervision of the entire arbitration process so as to assure the customer the equivalent of a trial by a "court of competent jurisdiction" [Section 12(2) of the Securities Act], including enforced adherence to the statutory shift in the burden of proof. The contrary assumption of the majority below appears to us to ignore the realities of the situation, as the dissenting opinion shows (R. 50-51). Moreover, since the suggestion concerning possible judicial supervision of the whole arbitration process is contrary to the views of other courts of appeals,[16] and those of the Court of Appeals for the Second Circuit in other cases,[17] there is no assurance that even the limited safeguards which the majority below suggests should be afforded through judicial super-

---

[16] See, *e.g.*, *Donahue* v. *Susquehanna Collieries Co.*, 160 F. 2d 661, 664 (C.A. 3) (district judge may not "supervise and control" the arbitration proceeding by directing findings on specified questions); *United Fuel Gas Co.* v. *Columbian Fuel Corp.*, 165 F. 2d 746, 751 (C.A. 4) (had the arbitrators misinterpreted the contract or considered improper evidence "this would not vitiate the award").

[17] See *American Almond Products Co.* v. *Consolidated Pecan Sales Co.*, 144 F. 2d 448, 451 (award confirmed despite plaintiff's failure to submit evidence on amount of damages; arbitrators may have determined amount by own expert knowledge and experience; when parties choose to arbitrate "they may not hedge it about with those procedural limitations which it is precisely its purpose to avoid"); *James-Richardson & Sons, Ltd.* v. *W. E. Hedger Trans. Co.*, 98 F. 2d 55, 57, certiorari denied, 305 U. S. 657 (court has no "power to amend or overrule merely because of disagreement with matters of law or fact determined by the arbitrators"); *In re Canadian Gulf Line, Ltd.*, 98 F. 2d 711, 714 (arbitration tribunal's "extensive powers" are subject to "most restricted review"). See also *Karppinen* v. *Karl Keifer Machine Co.*, 187 F. 2d 32, 34.

vision and review of the results of arbitration will be recognized elsewhere, or, for that matter, recognized in the court below when an award is actually challenged.

Instead of assuring the customer his statutory rights, including that of having the burden of proof shifted to the seller, the decision below imposes upon the customer the burden of proving, as a prerequisite to having an adverse award vacated, that the arbitrators did not comply with the requirements of the Securities Act.[18] This provides further evidence that the procedure sanctioned below is not an adequate substitute for the remedy afforded by the Securities Act. It illustrates, also, the lack of warrant for the majority's assumption that arbitration will be more "speedy" (R. 47); for, as the dissent aptly stated, "no matter how time consuming may be the arbitration itself, [under the majority's view] it must necessarily be succeeded by lengthy judicial proceedings before the award is legally enforceable" (R. 51). The arbitration award might then very well become the "commencement, not the end, of [the] litigation."[19]

CONCLUSION

The decision below presents a question as to the proper construction of the civil liabilities and anti-waiver provisions of the Securities Act of 1933

---

[18] *American Almond Products Co.* v. *Consolidated Pecan Sales Co., Inc.*, 144 F. 2d 448, 450 (C.A. 2).

[19] *Burchell* v. *Marsh*, 58 U.S. 344, 349.

which is of great importance to the investing public. For the reasons stated, we believe that the decision is erroneous, frustrates the policy of the Securities Act, and opens the door to nullification of important rights which Congress intended to afford public investors. Review by this Court seems clearly desirable in the public interest.

The petition for a writ of certiorari should be granted.

Respectfully submitted,

ROBERT L. STERN,
Acting Solicitor General.

ROGER S. FOSTER,
General Counsel,
ALEXANDER COHEN,
Special Counsel,
GEORGE H. JAFFIN,
Attorney,
Securities and Exchange Commission.

APRIL, 1953.

In the Supreme Court of the United States

OCTOBER TERM, 1952

No. 715

ANTHONY WILKO, PETITIONER

v.

JOSEPH E. SWAN, ET AL., INDIVIDUALLY AND DOING BUSINESS UNDER THE FIRM NAME AND STYLE OF HAYDEN STONE AND CO., ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY OF SECURITIES AND EXCHANGE COMMISSION, AMICUS CURIAE, TO BRIEF IN OPPOSITION

The Solicitor General on behalf of the Securities and Exchange Commission, *amicus curiae,* submits the following statement in reply to respondents' first point that the decision below is interlocutory and that the case is "not ripe for review." *Shanferoke Coal and Supply Corp.* v. *Westchester Service Corp.,* 293 U. S. 449, relied upon by respondents below to sustain the jurisdiction of the Court of Appeals, supports both

256455—53

the appealability of the district court's order and the propriety of review in this Court, assuming of course that the issue in other respects warrants certiorari as contended in our main brief. Had petitioner omitted to seek further review of the decision below, or should this Court fail to disturb that ruling, respondents would be in a position to urge that the issue presented by this petition is res judicata in any court proceeding which might follow an arbitration award unacceptable to petitioner. Cf. *American Surety Co.* v. *Baldwin*, 287 U. S. 156, 166–7; *United States* v. *Munsingwear*, 340 U. S. 36. In any event, we believe that whether petitioner should be permitted to pursue his statutory remedy under the Securities Act or be relegated to the substitute procedure of arbitration presents an issue which ought to be resolved before, rather than after, a trial on the merits. Certainly petitioner is as much prejudiced by the decision of the Court of Appeals, if erroneous, as respondents were prejudiced by the assumed erroneous holding of the district court. In the *Shanferoke* case, as in the present case, the district court had denied a stay of proceedings pending arbitration but had been reversed by the Court of Appeals. This Court not only upheld the appellate jurisdiction of the

Court of Appeals, but granted certiorari and reviewed the case on the merits.

Respectfully submitted.

ROBERT L. STERN,
Acting Solicitor General.

ROGER S. FOSTER,
General Counsel,
ALEXANDER COHEN,
Special Counsel,
GEORGE H. JAFFIN,
Attorney,
Securities and Exchange Commission.

MAY 1953.

U. S. GOVERNMENT PRINTING OFFICE: 1953

INDEX

	Page
Opinions below	1
Jurisdiction	2
Question presented	2
Statutes involved	3
Statement	6
Specification of errors	11
Summary of argument	11
Argument	15
I. Congress intended, and public policy requires, that the special judicial remedy afforded by Section 12(2) of the Securities Act be available to a customer seeking relief from a fraudulent sale	15
(a) Section 12(2) affords the customer a more effective judicial remedy than that accorded by common law	15
(b) The pre-sale attempt to deprive the customer of his Section 12(2) remedy conflicts with the purpose of the statute, and is rendered void by the anti-waiver provisions of Section 14	18
(c) Apart from Section 14, public policy precludes enforcement of the pre-sale stipulation since the Section 12(2) remedy is affected with a public interest	23
(d) Recognition of the pre-sale stipulation is not required by the Federal Arbitration Act	26
II. Arbitration cannot assure the customer his statutory rights	30
III. The possibility of valid post-controversy agreements, involving different statutory considerations, provides no basis for recognition of the pre-sale stipulation	44
Conclusion	48
Appendix—Margin Agreement	49

CITATIONS

Cases: Page

Ackerly v. *New York Central Railroad Co.*, 168 F. 2d 812 .....22, 23
Agostini Bros. Building Corp. v. *United States*, 142 F. 2d 854..... 26
American Almond Products Co. v. *Consolidated Pecan Sales Co. Inc.*, 144 F. 2d 448 .....35, 42, 43
Appel v. *Levine*, S.D. N.Y., Civ. Action No. 46-662, Sept. 20, 1948 30
Barnes v. *Youngs*, [1898] 1 Ch. 414 29
Boyd v. *Grand Trunk Western Railroad Co.*, 338 U. S. 263 20, 21, 22, 45, 46
Brooklyn Savings Bank v. *O'Neil*, 324 U. S. 697 .....23, 24, 25, 45
Burchell v. *Marsh*, 17 How. 344 44
Cackett v. *Keswick*, [1902] 2 Ch. 456 18
Callen v. *Penna. R.R.*, 332 U. S. 625 46
Campbell v. *American Fabrics Co.*, 168 F. 2d 959 40
Canadian Gulf Line, Ltd., In re, 98 F. 2d 711 .....35, 42
Cohen, Application of, 183 Misc. 1034, 52 N.Y.S. 2d 671, affirmed, 269 App. Div. 663, 53 N.Y.S. 2d 467, leave to appeal denied, 269 App. Div. 690, 54 N.Y.S. 2d 389, 294 N.Y. 640, 61 N.E. 2d 459 27-28
Czarnikow v. *Roth, Schmidt & Co.*, [1922] 2 K.B. 478 36
Diamond, Application of, 80 N.Y.S. 2d 465, affirmed, 274 App. Div. 762, 79 N.Y.S. 2d 924 27
Donahue v. *Susquehanna Collieries Co.*, 138 F. 2d 3 .....27, 28, 39
Donahue v. *Susquehanna Collieries Co.*, 160 F. 2d 661 42
Evans v. *Hudson Coal Co.*, 165 F. 2d 970 39
Gale, In re, 176 Misc. 277, 27 N.Y.S. 2d 18 39
Garrett v. *Moore-McCormack Co., Inc.*, 317 U. S. 239 17
Green v. *Howell*, [1910] 1 Ch. 495 29
Greenwood v. *Leather Shod Wheel Co.*, [1900] 1 Ch. 421 18
Hartbridge, The, 62 F. 2d 72, certiorari denied, 288 U. S. 601.... 42
Hill v. *Hill*, 199 Misc. 1035, 104 N.Y.S. 2d 755 28
James Richardson & Sons, Ltd. v. *W. E. Hedger Trans. Co.*, 98 F. 2d 55, certiorari denied, 305 U. S. 657 42
Jefferson Lake Sulphur Co. v. *Walet*, 104 F. Supp. 20, affirmed, *Walet* v. *Jefferson Lake Sulphur Co.*, 202 F. 2d 433, petition for certiorari filed June 24, 1953, No. 140 23
Kaiser-Frazer Corp. v. *Otis & Co.*, 195 F. 2d 838, certiorari denied, 344 U. S. 856 23
Karppinen v. *Karl Keifer Machine Co.*, 187 F. 2d 32 43
Kingswood Management Corp. v. *Salzman*, 272 App. Div. 328, 70 N.Y.S. 2d 692 27
Krenger v. *Pennsylvania Railroad Co.*, 174 F. 2d 556, certiorari denied, 338 U. S. 866 .....21, 45, 46
Kulukundis Shipping Co. v. *Amtorg Trading Corp.*, 126 F. 2d 978 32
Loving & Evans v. *Blick*, 204 P. 2d 23 (Cal.) 39

Page

Lumsden v. *Lumsden Bros. & Taylor, Inc.*, 242 App. Div. 852, 275 N.Y. Supp. 221 28
Murphy v. *Cady*, 30 F. Supp. 466, affirmed, 113 F. 2d 988, certiorari denied, 311 U. S. 705 17
Newburger v. *Lubell*, 257 N. Y. 213, 177 N. E. 424 30
O'Connell v. *Mallory*, S.D. N.Y., Civ. Action No. 47-164, March 22, 1949, CCH Fed. Sec. L. Rep. ¶ 90,445 30
Parry v. *Bache*, 125 F. 2d 493 29
Pittsburgh Const. Co. v. *West Side Belt R. Co.*, 151 Fed. 125.... 39
Quarrington Court, The, 102 F. 2d 916, certiorari denied *sub nom. Court Line, Ltd.* v. *Isthmian S.S. Co.*, 307 U. S. 645..... 28
Securities and Exchange Commission v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344 23
Springs Cotton Mills v. *Buster Boy Suit Co., Inc.*, 275 App. Div. 196, 88 N.Y.S. 2d 295, affirmed, 300 N. Y. 586, 89 N. E. 2d 877 ..... 40, 43
Swislocki v. *Spiewak*, 273 App. Div. 768, 75 N.Y.S. 2d 147 28
United Fuel Gas Co. v. *Columbian Fuel Corp.*, 165 F. 2d 746....40, 42
Wallis v. *Hirsch*, (1856) 26 L.J.C.P. 72 29
Watkins v. *Hudson Coal Co.*, 151 F. 2d 311, certiorari denied, 327 U. S. 777 ..... 26, 38
Wilkins v. *Allen*, 169 N. Y. 494, 62 N. E. 575 43
W. J. McCahan Sugar Refining and Molasses Co. v. *Stoffel*, 41 F. 2d 651 25
Workman v. *Belfast Harbour Commrs.*, [1899] 2 Ir. R. 234..... 29
Zip Mfg. Co. v. *Pep Mfg. Co.*, 44 F. 2d 184 ..... 24, 32

STATUTES:

Fair Labor Standards Act of 1938, 52 Stat. 1060, 29 U.S.C. § 201, *et seq.* 23

Federal Arbitration Act, 43 Stat. 883:
9 U.S.C. § 3 ..... 5, 12
9 U.S.C. § 10 ..... 2, 5, 36, 38

Federal Employers' Liability Act, 35 Stat. 65, as amended:
Section 5, 45 U.S.C. § 55 21
Section 6, 45 U.S.C. § 56 21

Securities Act of 1933, 48 Stat. 74, as amended:
Section 5, 15 U.S.C. § 77e 46
Section 11, 15 U.S.C. § 77k 17, 47
Section 12(2), 15 U.S.C. § 77l(2) 3, 11, 12, 15, 16, 18, 25, 41
Section 14, 15 U.S.C. § 77n 4, 11, 12, 18, 19, 22, 26
Section 16, 15 U.S.C. § 77p 15
Section 22(a), 15 U.S.C. § 77v(a) 4, 18

Page

Securities Exchange Act of 1934, 48 Stat. 881, as amended:
Section 7(a), 15 U.S.C. § 78g(a) 30
Section 16(b), 15 U.S.C. § 78p(b) 23
Section 29(a), 15 U.S.C. § 78cc(a) 23

New York Civil Practice Act:
Section 1466 43

English Arbitration Statute, 14 Geo. VI, c. 27:
Section 21 36
Section 24(2) 29

Legislative History:
H. Rep. No. 96, 68th Cong., 1st Sess. (1924) 38
H. Rep. No. 85, 73d Cong., 1st Sess. (1933) 15, 16, 19, 25
S. Rep. No. 47, 73d Cong., 1st Sess. (1933) 15

Articles, Texts, etc.:
American Arbitration Association, Commercial Arbitration Rule 30 41
Chamber of Commerce of the State of New York, *Handbook and Guide to Commercial Arbitration* (1932), pp. 4-6 32
Cohen and Dayton, *The New Federal Arbitration Law*, 12 Va. L. Rev. 265 (1926) 32
53 Col. L. Rev. 735 (1953) 1
41 Geo. L. J. 565 (1953) 1
66 Harv. L. Rev. 1326 (1953) 1, 42
Jacquin, *Arbitration on the Big Board*, Arbitration in Action, vol. 1, no. 2, p. 5 (1943) 32
Frank, *Courts on Trial* (1949), p. 377 31
Loss, *Securities Regulation* (1951) 16, 17, 18

New York Stock Exchange:
Constitution, Art. VIII, Sections 4 and 6 34
Rules of the Board of Governors, Rule 754 34
Russell, *Law of Arbitration* (15th ed., 1952), c. 12 36
Stone, *Justice Weighs Bulls and Bears*, Investment Dealers' Digest, Jan. 28, 1952, p. 20 32
62 Yale L. J. 985 (1953) 1

In the Supreme Court of the United States

October Term, 1953

No. 39

ANTHONY WILKO, *Petitioner*

v.

JOSEPH E. SWAN, et al., individually and doing business under the firm name and style of HAYDEN STONE AND CO., et al.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION, AMICUS CURIAE

OPINIONS BELOW

The opinion of the Court of Appeals (R. 40-49) is reported in 201 F. 2d 439 [1] The opinion of the District Court (R. 23-32) is reported in 107 F. Supp. 75.

[1] The Court of Appeals' decision is discussed in 62 Yale L. J. 985 (1953); 66 Harv. L. Rev. 1326 (1953); 53 Col. L. Rev. 735 (1953); 41 Geo. L. J. 565 (1953).

JURISDICTION

The judgment of the Court of Appeals was entered on January 15, 1953 (R. 52). The petition for a writ of certiorari was filed on April 14, 1953, and granted on June 1, 1953. 345 U. S. 969. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254. See also Section 22(a) of the Securities Act of 1933, 15 U.S.C. § 77v(a).

QUESTION PRESENTED

Whether an agreement to arbitrate an alleged cause of action under the civil liabilities provisions of Section 12(2) of the Securities Act of 1933, obtained by a securities firm from a customer at the initiation of their dealings, is valid and enforceable in view of the purpose of Congress to accord a defrauded purchaser the special statutory court remedy provided by Section 12(2), and in view of the provisions of Section 14 of that Act invalidating agreements to waive compliance with the statute.[2]

---

[2] The determination below also presents the question whether the provisions of the Federal Arbitration Act for vacating an award (9 U.S.C. § 10) empower a court to compel the arbitrators to comply with an agreement which (as construed by the court below) requires them to conduct the equivalent of a court proceeding. The Commission has no distinct statutory interest in the proper construction of the Federal Arbitration Act, but discusses this question to the extent that it is pertinent to the principal question set forth in the text.

STATUTES INVOLVED

The following are the pertinent provisions of the Securities Act of 1933, 48 Stat. 74, as amended:

Section 12(2), 15 U.S.C. § 771(2):

> Any person who—
>
> * * * * * *
>
> (2) sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission, shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such secu-

rity, or for damages if he no longer owns the security.

Section 14, 15 U.S.C. § 77n:

Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this title or of the rules and regulations of the Commission shall be void.

Section 22(a), 15 U.S.C. § 77v(a):

The district courts of the United States, the United States courts of any Territory, and the Supreme Court of the District of Columbia shall have jurisdiction of offenses and violations under this title and under the rules and regulations promulgated by the Commission in respect thereto, and, concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this title. Any such suit or action may be brought in the district wherein the defendant is found or is an inhabitant or transacts business, or in the district where the sale took place, if the defendant participated therein, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to re-

view as provided in sections 128 and 240 of the Judicial Code, as amended (U.S.C., title 28, secs. 225 and 347). No case arising under this title and brought in any State court of competent jurisdiction shall be removed to any court of the United States. * * *

The Federal Arbitration Act, 43 Stat. 883, provides:

9 U.S.C. § 3:

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

9 U.S.C. § 10:

In either of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration—

(a) Where the award was procured by corruption, fraud, or undue means.

(b) Where there was evident partiality or corruption in the arbitrators, or either of them.

(c) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced.

(d) Where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

* * * * * *

STATEMENT

This action was instituted by a customer against a securities firm to recover damages, under the civil liabilities provisions of Section 12(2) of the Securities Act of 1933, for alleged misrepresentations in the sale of securities. Petitioner, the customer, charged in his complaint that, on or about January 17, 1951, he was induced by the New York securities firm of Hayden, Stone and Co. to purchase 1,600 shares of the common stock of Air Associates, Inc., for $29,517.24, by false representa-

tions that Air Associates had concluded a contract of merger with the Borg Warner Corporation pursuant to which Air Associates stock would be valued at $23.50 per share, or $6.00 per share over the current market price, and that bankers and large financial interests were buying up Air Associates stock for participation in said merger. He was not told, he alleges, that one Haven B. Page, a director of, and counsel for, Air Associates, was then selling his own Air Associates stock, including some or all of the shares which were sold to petitioner. Page was also named as a defendant. Petitioner resold the stock two weeks later at a loss of $3,888.88. Claiming that this loss was due to the firm's misrepresentations, he sought damages in that amount (R. 2-4).

Without answering the complaint, the firm moved for a stay pursuant to the Federal Arbitration Act, 9 U.S.C. § 3, and filed an affidavit which disclosed that on May 2, 1950, apparently in connection with an earlier unrelated transaction, and again on January 18, 1951, in connection with the instant sale, petitioner had signed a form "Margin Agreement" which the firm used in its dealings with its customers (R. 7-10). The form agreement is reproduced in relatively large type in six pages of the Transcript of the Record (pp. 11-16); but the document attached to the affidavit was a fine-print form, approximately 8½ by 11 inches, containing on one side of the sheet numerous pro-

visions respecting the rights and liabilities of the parties. A photocopy of the executed form is attached to this brief as an Appendix. There is no indication in the record that the various provisions of the agreement were actually read by the petitioner, or explained to him, before his signature was obtained. The stated consideration for his agreement was simply the opening and maintenance of an account with the firm.

The seventeenth paragraph of this fine-print form contains the following provisions for compulsory arbitration (R. 16, 22):

> Any controversy arising between us under this contract shall be determined by arbitration pursuant to the Arbitration Law of the State of New York, and under the rules of either the Arbitration Committee of the Chamber of Commerce of the State of New York, or of the American Arbitration Association, or of the Arbitration Committee of the New York Stock Exchange or such other Exchange as may have jurisdiction over the matter in dispute, as I may elect. Any arbitration hereunder shall be before at least three arbitrators.

Another provision states that all transactions effected on the customer's behalf are subject to the constitutions, rules, customs and practices of the exchanges or markets where executed and of their

respective clearing houses, and to "the provisions of the Securities Exchange Act of 1934 and present and future acts amendatory thereof or supplemental thereto", and to applicable rules and regulations of the Securities and Exchange Commission (R. 11, 17).

Elsewhere in the fine-print form is a paragraph purporting to exculpate the firm and its members from liability for any misrepresentations made by them, or by their agents or employees, in the sale or purchase of securities (R. 14, 20).

The contract for the sale of the stock was a separate agreement (R. 26).

District Judge Goddard denied the motion for a stay pending arbitration. The arbitration agreement obtained by respondents "as a preliminary to the purchase of stock," he ruled, conflicted with the Securities Act of 1933 in attempting to deprive petitioner of the advantageous court remedy which Congress intended to afford a defrauded purchaser under Section 12(2) of that Act. Moreover, he held, it amounted to a waiver of compliance with the statute and was therefore rendered void by Section 14 of the Act (R. 23-32).

A divided Court of Appeals reversed the order of the District Court (R. 40-52). The majority of the court (Judges Swan and Chase) observed that the "question is not free from doubt" (R. 49), and described the district judge's opinion as "carefully reasoned" (R. 43) and one which "presents a

strong argument against the conclusion we have reached" (R. 49). It concluded, however, that the Securities Act of 1933 did not prohibit a securities firm from obtaining a pre-sale or pre-controversy agreement for the arbitration of any future cause of action, including the statutory cause of action for fraudulent misrepresentation, which a customer may later have reason to assert. The majority held, accordingly, that the stay provisions of the Federal Arbitration Act (9 U.S.C. § 3) were applicable (R. 41-49).

Judge Clark wrote a dissenting opinion in which he expressed the view that, under the ruling of the majority, "important rights under this notable first of a series of famous Acts for the benefit of the investing public [would] be capable of nullification by long fine-print restrictions of the broker's devising" (R. 52).

The Securities and Exchange Commission participated as *amicus curiae* in the proceedings in both courts below in opposition to the motion to stay the court action and compel arbitration, and also filed a brief in this Court in support of the petition for writ of certiorari. The Commission expresses no opinion with respect to any allegation of fact, or with respect to the substantive merits of the complaint.

SPECIFICATION OF ERRORS

While petitioner has assigned a sizable list of errors, the interest of the Commission as *amicus curiae* extends only to the following:

The majority of the Court of Appeals erred—

(1) In holding that the pre-sale agreement for compulsory arbitration is valid and enforceable against the petitioner customer in a subsequent action for fraudulent misrepresentation in the sale of securities brought against the respondent securities firm pursuant to Section 12(2) of the Securities Act of 1933; and, consequently,

(2) In reversing the order of the District Court which denied respondents' motion for a stay pending arbitration.

SUMMARY OF ARGUMENT

The decision below permits a securities firm—through the device of a fine-print pre-transaction agreement containing a compulsory arbitration clause—to deprive a customer of the special court remedy which Section 12(2) of the Securities Act of 1933 was intended to accord him in the event of a fraudulent sale. The arbitration provision should be held invalid because of conflict with the policy of Congress, and as an attempted waiver of the customer's statutory rights prohibited by Section 14 of that Act.

I.

The many litigation advantages provided by Section 12(2) were designed to afford a defrauded customer a simple and effective court remedy which he did not have at common law. The legislative history of Section 12(2), and the provisions of Section 14 invalidating waivers of compliance with the statute, make it clear that Congress intended this remedy to be available to a customer who seeks relief from a fraudulent sale. The view of the majority below that Section 14 only invalidates waivers of the "prohibitive provisions" of the Act, and not the "means of enforcement provisions", conflicts with the purpose and text of the statute, and imposes limitations upon broad statutory anti-waiver provisions which this Court has already rejected. Apart from the express anti-waiver provision, public policy precludes recognition of a stipulation limiting or preventing access to a court where, as here, the statutory rights, although conferred on a private party, are affected with a public interest.

The Federal Arbitration Act does not require recognition of the pre-sale stipulation; for that Act only pertains to controversies which are properly "referable to arbitration". The statute is inapplicable where public policy requires that the particular claim be decided by a court, or that the claimant have access to a court.

II.

The customer's statutory rights are not preserved in arbitration. The arbitration process is primarily suited for commercial disputes which often can best be resolved by businessmen on the basis of their own knowledge and experience, and without reference to technical rules of law. The Securities Act, on the other hand, was not intended to reflect business attitude toward the responsibilities of professionals in the securities field to their customers. The arbitrators would be appointed from an industry selected panel, and would ordinarily be laymen who could be expected to adjudicate the customer's claim without reference to the legal requirements of the Securities Act.

The suggestion of the majority below that it has safeguarded the customer's statutory rights by construing the pre-sale stipulation to require the arbitrators to apply the Securities Act rests upon a questionable legal premise and, in any event, is unrealistic. We know of no authority for the thesis of the majority below that the arbitrators can be compelled to abandon their normal functions and act like judges learned in the law through court review of an award to ascertain whether rules of legal procedure, evidence, and substantive law have been correctly applied. The suggested simulated court trial, moreover, conflicts with the various arbitration association rules adopted by the pre-

sale stipulation. The suggestion ignores the realities of the situation. The arbitrators will act according to their business background; and unless they volunteer explanations, which are not mandatory, there is no way of checking the steps by which they reach their conclusion.

III.

The assumption of the majority below that a post-controversy stipulation would be unobjectionable, and that a pre-sale stipulation presents no different question, overlooks important dissimilarities in relevant statutory policy. Election of a particular remedy or course of action, after a claim has been asserted, may possibly be consistent with the statutory scheme. A post-controversy stipulation for arbitration, if valid, would merely fall into the category of other post-controversy elections which may limit a plaintiff's course of action —*e.g.*, waiver of a jury trial, or acceptance of a compromise settlement. On the other hand, the pre-sale stipulation is designed to, and does, strip the customer of his statutory rights before there is any occasion for a choice of remedy.

ARGUMENT

I. Congress Intended, and Public Policy Requires, That the Special Judicial Remedy Afforded by Section 12(2) of the Securities Act be Available to a Customer Seeking Relief From a Fraudulent Sale.

(a) Section 12(2) Affords the Customer A More Effective Judicial Remedy Than That Accorded by Common Law.

A major purpose of the Securities Act of 1933 is to afford purchasers of securities more effective remedies for misrepresentation and non-disclosure than were accorded at common law.[3] Congress conceived that securities are "intricate merchandise",[4] and that the public interest demanded legislation which would recognize the gross inequality of bargaining power between the professionals in the securities business and the average investor. The Act was passed in response to a Presidential message urging that there be added to the ancient rule of *caveat emptor* the further doctrine "let the seller also beware",[5] and the reports of the Congressional committees recognize this important goal.[6] At the same time, deliberate consideration was given to avoidance of undue risks from errors of judgment by those engaged in the securities industry. Section 12(2) and the other civil liabili-

---

[3] The common law remedies, however, were preserved by Section 16 of the Act, 15 U.S.C. § 77p.

[4] H. Rep. No. 85, 73d Cong., 1st Sess. (1933), p. 8.

[5] *Id.* p. 2.

[6] *Ibid.*; S. Rep. No. 47, 73d Cong., 1st Sess. (1933), pp. 6-7.

tics provisions of the Securities Act must be read in this context.[7]

Under Section 12(2), the plaintiff is not required to prove *scienter* as he must at common law. On the contrary, the burden of proof is shifted to the defendant seller who must prove "that he did not know, and in the exercise of reasonable care could not have known of [the] untruth or omission." The legislative history discloses that Congress recognized that, as a practical matter, if more than mere "paper liability" was to be imposed upon fraudulent vendors of securities, "it is necessary to throw the burden of disproving responsibility for reprehensible acts of omission or commission" on the seller. H. Rep. No. 85, 73d Cong., 1st Sess. (1933), p. 9.[8] "To impose a lesser responsibility," it was felt, "would nullify the purposes of

---

[7] For a comprehensive discussion, see Loss, *Securities Regulation* (1951), pp. 996-1029.

[8] "The provisions * * * are indispensable to make the buyer's remedies * * * practically effective. Every lawyer knows that with all the facts in the control of the defendant it is practically impossible for a buyer to prove a state of knowledge or a failure to exercise due care on the part of the defendant." *Ibid.*

"The committee has deemed this shift in the burden of proof as both just and necessary, inasmuch as the knowledge of the seller as to any flaw in his selling statements or the failure of the seller to exercise reasonable care are matters in regard to which the seller may readily testify, but in regard to which the buyer is seldom in a position to give convincing proof." *Id.*, pp. 23-24.

this legislation." *Id.*, p. 10[9] In 1934, when in response to industry criticism Congress enacted some alleviating amendments with respect to Section 11 (civil liabilities on account of material misrepresentations or omissions in registration statements), it left Section 12(2) untouched.[10]

The statute also affords the defrauded purchaser a broad choice of forum. He may sue in any court of competent jurisdiction—federal or state. If he sues in a state court, the action cannot be removed to a federal court; and if he elects to sue in a federal court he has a broad choice of venue, with the

---

[9] That such a shift in the burden of proof is not a mere matter of procedure, but goes to the very substance of the statutory right conferred, see *Garrett* v. *Moore-McCormack Co., Inc.*, 317 U.S. 239. That case involved an action by an injured seaman under the Jones Act for damages, and for maintenance and cure, which had been brought in a Pennsylvania state court. By way of defense, the shipowner produced a release executed by the seaman. The Pennsylvania court applied state law in holding that the seaman had not met the burden of proof required to invalidate the release. In reversing that holding, this Court found that the seaman had not been given "the full benefit of federal law" (*id.*, 243). "The right of the petitioner to be free from the burden of proof imposed by the Pennsylvania local rule," it stated, "inhered in his cause of action," and "was a part of the very substance of his claim" (*id.*, 249).

[10] See Loss, *Securities Regulation* (1951), pp. 1014-1018. The advantage of the Section 12(2) remedy over the common law action for fraud and deceit is illustrated by *Murphy* v. *Cady*, 30 F. Supp. 466 (D. Maine), affirmed, 113 F. 2d 988 (C.A. 1) certiorari denied, 311 U. S. 705, where the court dismissed the common law count of the compiaint but sustained the statutory action on the same allegations of fact.

privilege of nation-wide service of process, and he need not comply with the $3,000.00 requirement of diversity cases. See Section 22(a).

(b) The Pre-sale Attempt to Deprive the Customer of His Section 12(2) Remedy Conflicts With the Purpose of the Statute, and Is Rendered Void by the Anti-waiver Provisions of Section 14.

That Congress intended this advantageous judicial remedy to be available to a customer seeking relief from a fraudulent sale, irrespective of private agreement to the contrary, is shown by the aforementioned legislative history, and by the anti-waiver provisions of Section 14 of the Act. The latter expressly state that any "stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this title * * * shall be void."[11] Under the instant stipulation for arbitration, exacted at the initiation of the customer's dealings with the securities firm, the customer waives his right, in the event of a fraudulent sale, to the special court remedy provided by Section 12(2) and the statutory choice of

[11] In enacting Section 14 Congress had the benefit of English experience in the securities field. Prior to the Companies Act of 1900, the English courts had honored stipulations binding securities purchasers to waive statutory liabilities so long as the stipulations were not too "tricky". *Greenwood* v. *Leather Shod Wheel Co.* [1900] 1 Ch. 421 (C.A.); *Cackett* v. *Keswick* [1902] 2 Ch. 456 (C.A.). For the past half-century, however, the English Companies Act has contained a broad non-waiver provision. See Loss, *Securities Regulation* (1951), pp. 1074-1077.

forum. We show below, in Point II, that arbitration does not assure the customer his statutory rights. The stipulation, in our opinion, involves to a very material degree a waiver of "compliance" with the statute.

The majority below, however, expressed the view that it was "far from clear that the words 'waive compliance with' refer to anything more than the mandatory or prohibitive provisions of the Act." It observed: "The means of enforcement provisions, on the other hand, seem clearly permissive, not requiring compliance" (R. 47). Section 14, of course, refers to "any provision of" the Act. To construe Section 14 as voiding only attempted waivers of the substantive prohibitions of the Act, such as those against fraud and misrepresentation, rather than the remedial provisions, runs counter to the express language of the section as well as to the evident purpose of the statute. Moreover, to the extent that enforcement of such substantive requirements is dependent upon the effectiveness of the private remedies afforded, the view of the majority below can only tend to undermine compliance with those substantive provisions as well. See H. Rep. No. 85, 73d Cong., 1st Sess. (1933), pp. 9-10, *supra*, pp. 16-17. Thus, if a customer, in advance of his dealings with a securities firm, may be induced to contract away all of his remedial rights under the Act, the obvious consequence is to render nugatory those remedies and to eliminate an im-

portant sanction relied upon by Congress to enforce compliance with the statute. The majority below clearly indicated that had the pre-sale stipulation provided for the waiver of all of the customer's remedial rights, it would have regarded this as a waiver of compliance within the meaning of Section 14. The decision below, accordingly, must rest on the untenable thesis that it is permissible to obtain a waiver of some of the customer's remedial rights, but not all of them. However, if the language "waive compliance with any provision of this title" is not construed to cover the waiver of a remedial right, as such, there appears no logical stopping point short of the complete deprivation of a remedy. On the other hand, if the quoted language does cover remedial rights, it necessarily preserves all of them, and forbids any of them to be bargained away in advance of the transaction giving rise to the customer's claim.

In any event, the kind of distinction made by the majority below has already been rejected by this Court. In *Boyd* v. *Grand Trunk Western Railroad Co.*, 338 U.S. 263, the Court held invalid a stipulation restricting an employee's choice of venue in an action under the Federal Employers' Liability Act (45 U.S.C. § 51). Section 6 of that Act (45 U.S.C. § 56) permits suit in any one of several localities, including any district in which the defendant may be doing business. Like the stipulation in the instant case which purports to

deprive the customer of his choice of a court remedy, including the right to a jury trial, and to relegate him to a proceeding before arbitrators appointed from an industry selected panel, the stipulation in the *Boyd* case would have deprived the railroad employee of his choice to sue the company wherever it was doing business, including suit in one of several large cities where jury verdicts might be higher, and would have limited him to an action in the locality where he resided or was injured. Section 5 of that statute (45 U.S.C. § 55) provides that any contract or device "to enable any common carrier to exempt itself from any liability created by this Act, shall to that extent be void * * *." The Court held that the "right to select the forum" is a "substantial right", and that the agreement which sought to restrict that choice "would thwart the express purpose of" the statute (338 U. S., at 266). See also the earlier case of *Krenger* v. *Pennsylvania Railroad Co.*, 174 F. 2d 556, certiorari denied, 338 U. S. 866, decided by the Court of Appeals for the Second Circuit, in which Judge Clark concluded that the term "liability", as used in the anti-waiver provisions of the Federal Employers' Liability Act, was not limited to the carrier's ultimate obligation to pay damages, but included the "liability to be sued, *i.e.*, to have its legal relations changed—adversely—in any one of several jurisdictions" (174 F. 2d, at 559). Restriction of the employee's choice of

venue, therefore, was viewed as an attempt to obtain exemption from liability for suit "except under the favoring conditions of a single chosen jurisdiction" (*ibid.*). In *Ackerly* v. *New York Central Railroad Co.*, 168 F. 2d 812, also decided before the *Boyd* case, the Court of Appeals for the Sixth Circuit had adopted a similar view. Rejecting the railroad's contention that its liability "is in no way affected by the place or forum of trial", Judge Allen stated that it "was liable under § 6 of the Act to be sued in any one of three jurisdictions" and that, accordingly, "the venue provision (was) an inherent part of the employer's liability" (168 F. 2d, at 814-815). The anti-waiver language of the Securities Act of 1933, is, if anything, broader than that of the Federal Employers' Liability Act; for it renders void waiver of "compliance with any provision of" the Act. There is no comparable basis under the Securities Act for the contention, which was made under the Federal Employers' Liability Act but rejected by this Court in the *Boyd* case, that Congress intended only to prohibit a waiver of the substantive liability for damages.

The majority below also concluded that Congress would have included in Section 14 of the Securities Act a specific prohibition against arbitration had it intended that section to have such broad coverage (R. 51). Congress saw fit, however, to cover the matter of waivers by a single broadly worded prohibition, as another panel of judges of

the Court of Appeals previously recognized (*Kaiser-Frazer Corp.* v. *Otis & Co.*, 195 F. 2d 838, 843, n. 8, certiorari denied, 344 U. S. 856), rather than by the particularization of specific types of waivers. *Cf. Jefferson Lake Sulphur Co.* v. *Walet*, 104 F. Supp. 20 (E.D. La.), affirmed, *Walet* v. *Jefferson Lake Sulphur Co.*, 202 F. 2d 433 (C.A. 5), petition for certiorari filed June 24, 1953, No. 140.[12] See also *Securities and Exchange Commission* v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344, 350.

(c) Apart from Section 14, Public Policy Precludes Enforcement of the Pre-Sale Stipulation Since the Section 12(2) Remedy is Affected With a Public Interest.

Wholly apart from the inclusion of an express anti-waiver provision in a statute, public policy prohibits the recognition and enforcement of stipulations limiting or preventing access to the courts where the statutory rights involved, although conferred on a private party, are affected with a public interest. *Brooklyn Savings Bank* v. *O'Neil*, 324 U. S. 697; *Ackerly* v. *New York Central Railroad Co.*, 168 F. 2d 812 (C.A. 6). In the *Brooklyn Savings Bank* case, this Court declared invalid a release waiving an employee's right to liquidated damages under the Fair Labor Standards Act. The

---

[12] The same anti-waiver language in Section 29(a) of the companion Securities Exchange Act of 1934, 15 U.S.C. § 78cc(a), was held in that case to make it "crystal clear" that any waiver of the right of a corporation to maintain an action under Section 16(b) of that statute, 15 U.S.C. § 78p(b), to recover the "short term" trading profits of a corporate insider, would be void (104 F. Supp., at 23-24).

liquidated damages provided by that statute were intended to compensate the employee for injury resulting from the improper retention of his pay which might be too difficult to estimate or prove. Underlying the Court's decision was the public interest which the statute sought to further—*viz.*, alleviation of "the unequal bargaining power as between employer and employee" which often resulted in employment agreements detrimental to the "national health and efficiency" and to the "free movement of goods in interstate commerce" (*id.*, 706-7). The rights given the employee were deemed to be of a "private-public character" related in purpose to, and supplementing the criminal and injunctive provisions enforced by the Government (*id.*, 709). Knowledge by the employer that he cannot escape his statutory liability by taking advantage of the inferior bargaining position of the employee, said Mr. Justice Reed, "tends to insure compliance in the first place" (*id.*, 710). The Court placed little significance upon the fact that an express anti-waiver provision had been eliminated from a predecessor bill, or upon the further fact that various other federal statutes authorizing employees to sue for wages and damages contain specific anti-waiver provisions. The absence of such a provision, Mr. Justice Reed stated, does not prevent the Court from invalidating waivers "where the legislative

policy would be thwarted by permitting such contracts" (*id.*, 713).[13]

As previously shown, the special court remedy which Section 12(2) of the Securities Act affords a defrauded purchaser of securities is similarly affected with a public interest. A principal purpose of the statute was to curb the "wanton misdirection of the capital resources of the Nation" [14] which had resulted in large measure from sales of securities to the public without adequate disclosures of the relevant facts and frequently by positive misrepresentations. Section 12(2) and other provisions of the statute were designed to alleviate the existing gross inequalities between the professionals in the securities business and the average investor. Like the Federal Employers' Liability Act, enforcement is divided between the government and the injured investor. The special court remedies for rescission and damages afforded the latter serve to give the individual redress and, by their very existence, also act as a deterrent to violation of the statute, thereby supplementing the public enforcement functions of the Commission. Under this Court's ruling in the *Brooklyn Sav-*

---

[13] See also *W. J. McCahan Sugar Refining and Molasses Co.* v. *Stoffel*, 41 F. 2d 651 (C.A. 3), in which an agreement that an injured seaman's claim would be governed by the Pennsylvania Workmen's Compensation Law was held invalid as against public policy and, accordingly, no bar to the more advantageous suit under the Jones Act.

[14] H. Rep. No. 85, 73d Cong., 1st Sess. (1933), p. 3.

ings Bank case, circumvention of the investor's statutory remedies, so charged and colored with the public interest, cannot be sanctioned even apart from the express anti-waiver provisions of Section 14.

(d) Recognition of the Pre-Sale Stipulation Is Not Required by the Federal Arbitration Act.

The existence of the Federal Arbitration Act at the time of the passage of the Securities Act provides no basis for doubt that Congress intended that the Section 12(2) court remedy be an available choice of every customer who finds that he has been defrauded. The arbitration statute is applicable only to controversies which are properly "referable to arbitration". Where, as a matter of public policy, the dispute ought to be handled by the courts or where the claimant ought at least to have access to the courts, the controversy does not come within the intended purview of the arbitration statute. The applicable public policy, of course, may be determined by the courts or by the legislature.[15]

---

[15] The fact that the cause of action asserted may be statutory in origin, of course, does not necessarily mean that public policy forbids arbitration. Agreements to arbitrate claims under the Miller Act and Fair Labor Standards Act of 1938, for example, have been regarded as presenting no conflict with the policies of those statutes. See *Agostini Bros. Building Corp.* v. *United States*, 142 F. 2d 854 (C.A. 4); *Watkins* v. *Hudson Coal Co.*, 151 F. 2d 311 (C.A. 3), certiorari denied, 327 U. S. 777; *Donahue* v. *Susquehanna Col-*

In *Zip Mfg. Co.* v. *Pep Mfg. Co.*, 44 F. 2d 184 (D. Del.), a case under the federal arbitration statute, it was held that arbitration is not suitable for resolving a controversy involving the validity of a patent or the question of infringement. In *Kingswood Management Corp.* v. *Salzman*, 272 App. Div. 328, 70 N.Y.S. 2d 692, the New York arbitration law, upon which the federal statute was patterned,[16] was held inapplicable to a controversy involving an attorney's fee in a treble damages suit under the Federal Emergency Price Control Act.[17] In *Application of Diamond*, 80 N.Y.S. 2d 465, 467 (Sup. Ct.), affirmed, 274 App. Div. 762, 79 N.Y.S. 2d 924, a motion to stay a stockholder's derivative action and to require the claim to be resolved in an arbitration proceeding was denied on the ground, *inter alia*, that if the arbitration agreement covered the particular issues there involved it "would be unenforceable as against public policy". In *Application of Cohen*, 183

lieries Co., 138 F. 2d 3 (C.A. 3). The arbitrators' task in these cases was largely confined to making the necessary computations to ascertain amounts due the claimants. In the *Donahue* case the court agreed that arbitration would have been precluded had the legislative policy of the Fair Labor Standards Act been inconsistent therewith (138 F. 2d, at 6).

[16] *Zip Mfg. Co.* v. *Pep Mfg. Co.*, 44 F. 2d 184, 185 (D. Del).

[17] The Court stated (70 N.Y.S. 2d, at 693):

"The Emergency Price Control Act was adopted from urgent reasons of public policy which the Congress did not intend to turn over to private arbitrators to administer."

Misc. 1034, 52 N.Y.S. 2d 671 (Sup. Ct.), affirmed, 269 App. Div. 663, 53 N.Y.S. 2d 467,[18] a stay pending arbitration was denied in a proceeding to dissolve a closed corporation because of disagreement of the parties. *Cf.* also, *Lumsden* v. *Lumsden Bros. & Taylor, Inc.*, 242 App. Div. 852, 275 N.Y. Supp. 221. The New York arbitration statute has also been held inapplicable in other instances where it was determined that public policy required that the matter be subjected to judicial surveillance. Thus, arbitration has been deemed inappropriate as respects the custody of children and rights of visitation, *Hill* v. *Hill*, 199 Misc. 1035, 104 N.Y.S. 2d 755 (Sup. Ct.), and, as respects the distribution of a decedent's estate, *Swislocki* v. *Spiewak*, 273 App. Div. 768, 75 N.Y.S. 2d 147. See also *The Quarrington Court*, 102 F. 2d 916 (C.A. 2), certiorari denied, *sub nom. Court Line, Ltd.* v. *Isthmian S.S. Co.*, 307 U.S. 645, where it was held that the federal statute did not authorize arbitration of one of several claims subject to a limitation proceeding in admiralty.

It may be relevant to observe, also, that the more elaborate English arbitration statute now in effect contains a provision which expressly empowers the court to disregard an agreement for arbitration where, as in the instant case, an issue of fraud

---

[18] Leave to appeal denied, 269 App. Div. 690, 54 N.Y.S. 2d 389, 294 N.Y. 640, 61 N. E. 2d 459.

is to be resolved.[19] Even before that provision, however, the English courts had regarded fraud claims as generally unfit for arbitration.[20] The suggestion of the majority below that its decision is in harmony with the English law (R. 48, n. 9), accordingly, would appear to be erroneous. See also pp. 36-38, *infra*.

We know of no prior precedent for permitting the waiver, through an arbitration agreement, of the statutory remedies provided in the Securities Act of 1933. Neither of the two cases in the securities field relied upon by respondents in the court below, and in which arbitration was required, involved an action under the federal securities statutes; and both cases presented essentially commercial disputes. One of them, *Parry* v. *Bache*, 125

---

[19] Section 24(2) of the English Arbitration Statute of 1950 (14 Geo. VI, c. 27) provides:

"Where an agreement between any parties provides that disputes which may arise in the future between them shall be referred to arbitration, and a dispute which so arises involves the question whether any such party has been guilty of fraud, the High Court shall, so far as may be necessary to enable that question to be determined by the High Court, have power to order that the agreement shall cease to have effect and power to give leave to revoke the authority of any arbitrator or umpire appointed by or by virtue of the agreement."

[20] *Wallis* v. *Hirsch*, (1856) 26 L.J.C.P. 72, 73 (Cockburn, C. J.: "The plaintiffs allege that a gross fraud has been practised on them; and we do not think that is a proper question to be referred to two brokers."); *Barnes* v. *Youngs*, [1898] 1 Ch. 414, 419; *Green* v. *Howell*, [1910] 1 Ch. 495, 511 (C.A.). See also *Workman* v. *Belfast Harbour Commrs.*, [1899] 2 Ir. R. 234, 245 (Q.B. Div.).

F. 2d 493 (C.A. 5), was an action for an accounting with reference to securities which defendant was authorized to buy and sell on behalf of the plaintiff; the other *Newburger* v. *Lubell*, 257 N.Y. 213, 177 N.E. 424, decided prior to the Securities Act, involved the propriety of a broker's action in closing out a customer's account. [21]

II. Arbitration Cannot Assure the Customer His Statutory Rights.

The district court and Judge Clark dissenting in the court below correctly pointed out that arbitration cannot assure a customer that his statutory rights will be safeguarded. The advantages of arbitration as a simple and speedy method of disposing of commercial disputes which can satisfactorily, and often best, be determined by persons expert in the particular business in light of their own experience and knowledge, and without reference to technical rules of law and procedure, provide the

---

[21] In the court below we called attention to two unreported district court decisions which enforced arbitration agreements involving claims arising out of alleged violations of the margin rules promulgated by the Federal Reserve Board under Section 7(a) of the Securities Exchange Act of 1934, 5 U.S.C. § 78g(a). *Appel* v. *Levine*, S.D. N.Y., Civil Action No. 46-662, Sept. 20, 1948 (Clancy, J.), and *O'Connell* v. *Mallory*, S.D.N.Y., Civ. Action No. 47-164, March 22, 1949 (Kaufman, J.), CCH Fed. Sec. L. Rep. § 90, 445. There was no contention or discussion in either case as to the validity of the arbitration agreement, and the question which might have been presented would in any event be dissimilar because of the differences in statutory context. The majority below did not deem these decisions sufficiently relevant to be cited.

basis for the rapid growth of these nonjudicial tribunals in recent years.[22] In the words of leading proponents—

> It is a remedy peculiarly suited to the disposition of the ordinary disputes between merchants as to questions of fact—quantity, quality, time of delivery, compliance with terms of payment, excuses for nonperformance, and the like. It has a place also in the determination of the simpler questions of law—the questions of law which arise out of these daily relations between merchants as to the passage of title, the existence of warranties, or the questions

---

[22] Compare Judge Frank's observation in his recent book, *Courts on Trial* (1949), p. 377:

"Since, generally speaking, arbitrators are not bound to apply legal rules, the fact that, increasingly, businessmen resort to arbitration throws some doubt on the conventional notion * * * that precise legal rules are primarily needed in the realm of business, that they supply a certainty and stability which men of business must have, that 'the commercial world' demands such rules 'because no one * * * engages in complex commercial undertakings trusting to' decisions resting on uncertain exercise of 'discretion'. Paradoxically, arbitration, with its freedom to disregard the legal rules, seems to function best in dealing with business disputes and not with those disputes which arise from angry personal feelings—where, on the whole, legal certainty has been said to be as of far less importance. One suggested explanation of this paradox is that businessmen who arbitrate have less interest in the legal rules than in the customs of their trade, which they feel will receive more attention from arbitrators acquainted with those trade customs than from the courts."

of law which are complementary to the questions of fact which we have just mentioned.[23]

In the securities field, it has been employed as a means of settling a variety of technical and business disputes—*e.g.*, controversies relating to the handling of customers' orders and securities, disputes between broker-dealers, disputes between partners in securities firms, and so forth.[24]

But even the proponents of arbitration have cautioned that arbitration should not be regarded as a desirable substitute for a court trial in many types of cases. See *Handbook and Guide to Commercial Arbitration,* issued by the Chamber of Commerce of the State of New York (1932), pp. 4-6. Where expertise in the law, rather than experience in a particular phase of business, is essential to a proper determination of the particular controversy, the arbitration process may be fraught with danger.[25] "The power to disregard rules of procedure and evidence and of law, which is one of the great advantages of proper arbitra-

---

[23] Cohen and Dayton, *The New Federal Arbitration Law,* 12 Va. L. Rev. 265, 281 (1926), quoted with approval in *Zip Mfg. Co.* v. *Pep Mfg. Co.*, 44 F. 2d 184, 186 (D. Del.).

[24] See Jacquin, *Arbitration on the Big Board,* Arbitration in Action, vol. 1, no. 2, p. 5 (1943); Stone, *Justice Weighs Bulls and Bears,* Investment Dealers' Digest, Jan. 28, 1952, p. 20. See also pp. 29-30, *supra.*

[25] *Cf.* Judge Frank's remarks in *Kulukundis Shipping Co.* v. *Amtorg Trading Corp.*, 126 F. 2d 978, at 987, n. 32 (C.A. 2).

tion, is capable of becoming an instrument of abuse and oppression in such hands (i.e., in the hands of laymen)—just as a motor car driven by an unskilled * * * driver can do great damage." *Id.*, p. 6.

The Securities Act of 1933 was not intended to reflect business custom as to the responsibility of professionals in the securities business with repect to representations made to customers. Rather, it was designed primarily to protect the less informed members of the public against the professionals, in the light of past experience which indicated that misrepresentations not infrequently were made and that under pre-existing law it was extremely difficult for the customer to obtain adequate redress. To that end, the 1933 Act affords the customer who believes he has been sold securities through misrepresentation a court remedy in which the seller is deprived of important legal advantages which he had at common law, and, most significantly, is required to prove his innocence once the customer establishes the misrepresentation. In addition, the statute gives the customer a choice between suing in a federal court or in a state court, as well as a liberal choice of venue. Such provisions for investor protection become quite innocuous if the professional may deprive the customer of these rights by obtaining, in advance of any controversy, the customer's signature to a fineprint agreement purporting to take away from him his judicial remedies under the statute, and relegating

him to a proceeding before an industry selected board of arbitrators.[26]

We do not believe that it was intended that the court remedy provided by the statute could be rendered unavailable to a customer by a form agreement, prepared by the seller's attorney, whether or not the seller or his attorney deemed the substitute procedure of arbitration more advantageous for the seller, or more advantageous for both the seller and the customer. For that reason, we regard as irrelevant respondents' argument that arbitration is as good for the customer as is court litigation. Clearly it is different, or there would be no point in exacting the stipulation to arbitrate; and respondents' present insistence upon arbitration indicates that they consider the differences advantageous to them. Among the aspects of the court remedy provided by the statute, which are not available to the customer in arbitration, are the rights to have questions of law decided by a judge subject to appellate review, to have issues of fact established by competent and relevant evidence, and to have such issues determined by a jury unless a jury trial is waived. In arbitration, however, as Judge Learned Hand has stated, the parties "must content themselves with looser approximations to the enforcement of their

---

[26] See *e.g.*, Art. VIII, Sections 4 and 6, of the Constitution, and Rule 754 of the Rules of the Board of Governors, of the New York Stock Exchange.

rights than those that the law accords them, when they resort to its machinery." *American Almond Products Co.* v. *Consolidated Pecan Sales Co., Inc.*, 144 F. 2d 448, 451 (C.A. 2).[27] As previously indicated, the arbitrators would ordinarily be laymen who would hear and decide the customer's claim without reference to technical rules of law and procedure. There is no assurance that the arbitrators would or could correctly apply the rules of procedure, the principles of evidence, the substantive law of fraud and misrepresentation, the statutory burden of proof, and the correct measure of damages. There is no assurance, moreover, that lay arbitrators would not be influenced in some degree by the exculpatory provision of the margin agreement whose invalidity was recognized by the court below (R. 45, 48). Finally, as Judge Clark observed in his dissent, it is improbable that industry arbitrators would give "the customer that objective and sympathetic consideration of his claim which is envisaged by the Securities Act" (R. 50).

The majority of the Court of Appeals was not unconcerned with these dangers. It felt, however, that they would be avoided in this case because (1) it construed the margin agreement to require, by implication, that the arbitrators apply the provi-

[27] To the same effect, see Judge Augustus N. Hand's remarks in *In re Canadian Gulf Line, Ltd.*, 98 F. 2d 711, 714 (C.A. 2).

sions of the Securities Act of 1933, and (2) it considered that, therefore, a decision by the arbitrators not reached in conformity with Section 12(2) could be vacated by the court under Section 10 of the Federal Arbitration Act, 9 U.S.C. § 10 (R. 45-46, 48-49). A persuasive authority, it noted, was the English decisional law under which "even without such an express provision in the arbitration agreement, the arbitrators must decide 'according to the legal rights of the parties' ", citing a number of English cases (R. 48, n. 9). The majority below, however, was apparently unaware of the provision in the English Arbitration Act which enables the court to render judgment on any question of law arising during the course of an arbitration proceeding, or on the legal correctness of an award or part of an award, upon a "special case" submitted by the arbitrator or directed by the court on application of a party.[28] The underlying rationale of the English arbitration statute is set forth in *Czarnikow* v. *Roth, Schmidt & Co.*, [1922] 2 K.B. 478 (C.A.), one of the cases cited by the majority below, holding invalid a provision in an arbitration agreement that questions of law arising in the course of the arbitration should be decided by the arbitrator. Lord Justice Scrutton stated (pp. 488-489):

---

[28] Section 21 of the English Arbitration Act (14 Geo. VI, c. 27) codifying earlier statutes. See Russell, *Law of Arbitration* (15th ed., 1952), c. 12.

Arbitrators, unless expressly otherwise authorized, have to apply the laws of England. When they are persons untrained in law, and especially when as in this case they allow persons trained in law to address them on legal points, there is every probability of their going wrong, and for that reason Parliament has provided in the Arbitration Act that, not only may they ask the Courts for guidance and the solution of their legal problems in special cases stated at their own instance, but that the Courts may require them, even if unwilling, to state cases for the opinion of the Court on the application of a party to the arbitration if the Courts think it proper. This is done in order that the Courts may insure the proper administration of the law by inferior tribunals. In my view to allow English citizens to agree to exclude this safeguard for the administration of the law is contrary to public policy. * * * I am ready to go very far in ignoring technicalities and irregularities on the part of arbitrators, unless there is some real substance of error behind them, but I think commercial men will be making a great mistake if they ignore the importance of administering settled principles of law in commercial disputes, and trust to the judgment of business men, however experienced in business, based only on the facts of each particular case, and with

no knowledge of or guidance in the principles of law which must control the facts and which arbitrators must administer.

Unlike the English statute, the Federal Arbitration Act does not authorize a court to decide questions of law arising during the course of an arbitration proceeding,[20] or to ascertain whether the arbitrators correctly applied the law in reaching their award. The court review provisions of Section 10 of the federal statute, upon which the majority below relied, empower the court to vacate an award for "corruption, fraud, or undue means", "evident partiality ", "misconduct" in refusing postponements or in refusing to hear "pertinent and material" evidence, or where the arbitrators have "exceeded their powers".

The simulated court trial which the majority below suggested would be required as the result of its construction of the margin agreement runs counter to the basic purpose and concept of the arbitration process. We know of no authority in the Federal Arbitration Act or elsewhere which would empower a court to compel arbitrators to abandon their normal functions and conduct the equivalent of a court proceeding, assuming that

---

[20] The House of Representatives' Report on the bill which became the Federal Arbitration Act noted that once the arbitration machinery is set in motion, "the arbitration proceeds without interference by the court". H. Rep. No. 96, 68th Cong., 1st Sess. (1924); p. 2.

they were able to do so. In support of its assumption that the failure of the arbitrators correctly to apply Section 12(2) would constitute a ground for vacating the award under Section 10 of the federal arbitration statute, the majority below cited but one case—*Evans* v. *Hudson Coal Co.*, 165 F. 2d 970 (C.A. 3). However, all that the Court of Appeals for the Third Circuit suggested in the *Evans* case was that an arbitration award based upon a wage formula in a collective bargaining contract which was clearly illegal under the Fair Labor Standards Act might be set aside.[30] An illegal provision, of course, cannot afford a basis for arbitration.[31] That court had concluded in earlier cases that there was nothing in the Fair Labor Standards Act which was inconsistent with the arbitration of claims under that statute (*Donahue* v. *Susquehanna Collieries Co.*, 138 F. 2d 3, 6), and that the "calculation of the amount of money to which * * * [an employee] may be entitled under the Act * * * is the kind of problem which is properly referable * * * to * * * an arbitrator" (*Watkins* v. *Hudson Coal Co.*, 151 F. 2d 311, 320, certiorari denied, 327 U.S. 777). In the *Evans* and

---

[30] This is enunciated more clearly in *Watkins* v. *Hudson Coal Co.*, 151 F. 2d 311 (C.A. 3), certiorari denied, 327 U.S. 777, to which the court referred.

[31] *Loving & Evans* v. *Blick*, 204 P. 2d 23, 27 (Cal.); *In re Gale*, 176 Misc. 277, 27 N.Y.S. 2d 18, 21-23 (Sup. Ct.); *Pittsburg Const. Co.* v. *West Side Belt R. Co.*, 151 Fed. 125, 130 (C.C. W.D. Pa.).

Watkins cases, the court set forth the correct legal standard for the guidance of the arbitrators in making their mathematical computations—a task it regarded as appropriate for lay arbitrators.[32]

As previously indicated, nowhere in the review provisions of the federal arbitration statute does there appear to be any authority vested in the courts to compel arbitrators to act like judges learned in the law through review of the award to ascertain whether the rules of legal procedure, evidence, or substantive law have been correctly interpreted and applied. Moreover, the pronouncement of the majority below gives no consideration to the various arbitration associations' rules ex-

[32] Nor do the additional cases cited by respondents in their brief opposing the grant of certiorari (pp. 13-14) provide support for the suggestion of the majority below. Thus, *Campbell* v. *American Fabrics Co.*, 168 F. 2d 959 (C.A. 2), and *United Fuel Gas Co.* v. *Columbian Fuel Corp.*, 165 F. 2d 746 (C.A. 4), both involved objections that the arbitrators had disregarded express contract formulas for the valuation of property. In the latter case, the court found that the arbitrators had not misinterpreted the contract nor considered improper evidence, but observed that "had they done so, this would not vitiate the award" (165 F. 2d, at 751). *Springs Cotton Mills* v. *Buster Boy Suit Co., Inc.*, 275 App. Div. 196, 88 N.Y.S. 2d 295, affirmed, 300 N.Y. 586, 89 N.E. 2d 877, cited under the New York arbitration statute, merely suggests that the arbitrators may be restricted by contract to consideration of only such evidence as the parties may themselves produce. The court regarded it as "well settled," however, that the arbitrators could not be hampered by adherence to the "case and statutory law governing the prosecution of actions" (88 N.Y.S. 2d, at 298).

pressly adopted by the Margin Agreement with which the required simulated court trial would appear to conflict.[33]

While we assume that an award which expressly relied upon the invalid exculpatory clause in the Margin Agreement could be set aside for that reason alone,[34] as a practical matter the possibility of judicial review of an award suggested by the court below cannot enable the court to exercise supervision of the entire arbitration process so as to assure the customer the equivalent of a trial by a "court of competent jurisdiction", to which he is entitled under Section 12(2) of the Securities Act, including enforced adherence to the statutory shift in the burden of proof. The contrary assumption of the majority below appears to ignore the realities of the situation. As Judge Clark aptly stated in his dissent (R. 50-51)—

> The suggestion that perhaps the business arbitrators will be able or inclined to manipulate the burden of proof like lawyers and judges seems to me completely unreal. * * * The arbitrators will act according to their business background and there will be no way

---

[33] Thus, the rules of the American Arbitration Association provide that "The Arbitrator shall be the judge of the relevancy and materiality of the evidence offered and conformity to legal rules of evidence shall not be necessary." Rule 30 of the Commercial Arbitration Rules.

[34] See n. 31, *supra*.

—unless they volunteer foolish explanations in their decision—of checking what they do.[35]

The suggestion concerning possible supervision of the whole arbitration process, moreover, appears inconsistent with the concept of the judicial function expressed by other courts of appeals,[36] and by the Court of Appeals for the Second Circuit itself in other cases,[37] so that it is not at all clear

---

[35] The suggestion in the Harvard Law Review (66 Harv. L. Rev. 1326) that review of the arbitrators' application of the statutory burden of proof would probably be no less than review of a jury verdict, overlooks the power of a trial judge to direct a verdict or to set aside a verdict as contrary to the weight of the evidence—a power not possessed by a reviewing court under the Federal Arbitration Act as respects an arbitration award.

[36] See *e.g.*, *Donahue* v. *Susquehanna Collieries Co.*, 160 F. 2d 661, 664 (C.A. 3), (district judge may not "supervise and control" the arbitration proceeding by directing findings on specified questions); *United Fuel Gas Co.* v. *Columbian Fuel Corp.*, 165 F. 2d 746, 751 (C.A. 4), *supra*, n. 32.

[37] See *American Almond Products Co.* v. *Consolidated Pecan Sales Co., Inc.*, 144 F. 2d 448, 451 (award confirmed despite plaintiff's failure to submit evidence on amount of damages; arbitrators may have determined amount by own expert knowledge and experience; when parties choose to arbitrate "they may not hedge it about with those procedural limitations which it is precisely its purpose to avoid"); *James Richardson & Sons, Ltd.* v. *W. E. Hedger Trans. Co.*, 98 F. 2d 55. 57, certiorari denied, 305 U.S. 657 (court has no "power to amend or overrule merely because of disagreement with matters of law or fact determined by the arbitrators"); *In re Canadian Gulf Line, Ltd.*, 98 F. 2d 711, 714 (arbitration tribunal's "extensive powers" are subject to "most restricted review"); *The Hartbridge*, 62 F. 2d 72, certiorari de-

that even the limited safeguards which the majority below suggests should be afforded through judicial supervision and review of the results of arbitration will be recognized elsewhere, or, for that matter, recognized in the court below when an award is actually challenged.

Instead of assuring the customer his statutory rights, including that of having the burden of proof shifted to the seller, the decision below imposes upon the customer the burden of proving, as a prerequisite to having an adverse award vacated, that the arbitrators did not comply with the requirements of the Securities Act.[38] This provides further evidence that the procedure sanctioned below is not an adequate substitute for the remedy afforded by the Securities Act. It illustrates, also, the lack of warrant for the majority's assumption that arbitration will be more "speedy" (R. 47);

---

nied, 288 U.S. 601 (arbitrators' determination either as to law or facts is final, award confirmed where no showing of fraud, corruption, misconduct, or action in excess of arbitrators' powers). See also *Karppinen* v. *Karl Keifer Machine Co.*, 187 F. 2d 32, 34.

To the same effect, under the similar court review provisions of the New York arbitration statute (N.Y. Civil Practice Act, § 1466), see *Springs Cotton Mills* v. *Buster Boy Suit Co., Inc.*, 275 App. Div. 196, 88 N.Y. Supp. 2d 295, affirmed, 300 N.Y. 586, 89 N.E. 2d 877, *supra* n. 32. See also *Wilkins* v. *Allen*, 169 N.Y. 494, 496, 62 N.E. 575, 576 ("The award of an arbitrator cannot be set aside for mere errors of judgment, either as to the law or as to the facts".)

[38] *American Almond Products Co.* v. *Consolidated Pecan Sales Co., Inc.*, 144 F. 2d 448, 450 (C.A. 2).

for, as the dissent aptly stated, "no matter how time consuming may be the arbitration itself, [under the majority's view] it must necessarily be succeeded by lengthy judicial proceedings before the award is legally enforceable" (R. 51). The arbitration award might then very well become the "commencement, not the end, of [the] litigation".[39]

III. The Possibility of Valid Post-Controversy Agreements, Involving Different Statutory Considerations, Provides No Basis for Recognition of the Pre-Sale Stipulation.

The assumption of the majority below (R. 46-7) that the customer could enter into a binding stipulation to arbitrate his claim after an action has been instituted, and that a pre-sale stipulation presents no different question, overlooks important differences in statutory policy. Since the Act accords the defrauded customer an election between his statutory and common law remedies, and gives him also a choice of forum, it may perhaps be arguable that it might be consistent with the purpose of the statute if the customer were permitted to elect, after an action has been commenced, to have his claim for violation of his substantive rights determined by arbitration rather than by court action. *The Commission took no position on this question in the court below and we take none here.* We suggest merely that if post-

---

[39] *Burchell* v. *Marsh*, 17 How. 344, 349.

controversy agreements to arbitrate are valid, they fall into the category of other post-controversy arrangements which may limit plaintiff's course of action, such as the decision to waive a jury trial, or perhaps to accept a compromise settlement of his claim. We submit, therefore, that the court below erred in assuming that there can be no distinction between a pre-controversy and a post-controversy stipulation. While we do not so argue at this time, we recognize the possibility that the grant of latitude for informed and reasonable post-controversy agreements may perhaps be consistent with the realistic effectuation of the purpose of Congress to afford the investor a choice of remedies.[40]

On the other hand, to uphold the pre-controversy stipulation enables the professional in the securities business to strip the investor of the protection of the statute. Contrary to the purpose of Congress, the decision below gives no recognition to the grossly unequal positions of the securities firm

---

[40] The fact that the stipulation is entered into after the cause of action has been asserted, of course, cannot in itself give it validity. Thus, the stipulations which this Court held invalid in the *Boyd* and *Brooklyn Savings Bank* cases (pp. 20-21, 23-25, *supra*) were obtained after causes of action had been asserted. Determination of the validity or invalidity of a post-controversy stipulation would require consideration of the particular statutory policy applicable to the rights abandoned. Moreover, as Judge Learned Hand suggested in the *Krenger* case (174 F. 2d, at 562), it might be advisable in any event to withhold judicial sanction if it does not appear that the claimant had the benefit of independent counsel before signing the agreement.

and the average customer who, before effecting a purchase, is requested to sign a fine-print form agreement.[41] An analogy on this point is mentioned in Judge Clark's minority opinion—*viz.*, the decisions of this Court which invalidate, under the Federal Employers' Liability Act, releases obtained prior to an accident, but recognize them if fairly and reasonably made in settlement of an existing claim (R. 52).[42] As Judge Clark noted, however, the question as to when a post-controversy agreement may be valid is not now before this Court.

Recognition of the pre-sale stipulation runs counter to the basic philosophy of the Securities Act that the statutory disclosure requirements be complied with before the customer is in any way committed in a securities transaction (see Section

---

[41] As District Judge Goddard observed, the average customer is unaware of his rights under the Securities Act and would not hesitate to sign what appears to him to be the "customary form" for opening an account with the securities firm (R. 28). The instant form, moreover, may lull an unsuspecting customer, who may happen to glance over it before signing, into a false sense of security. An early paragraph gives the impression that everything will be done in accordance with federal law—*viz.*, the Securities Exchange Act of 1934 and supplemental statutes. Later paragraphs, however, contain, *inter alia*, the broad exculpatory clause and the provision for compulsory arbitration.

[42] *Callen* v. *Penna. R. R.*, 332 U.S. 625, 631; *Boyd* v. *Grand Trunk Western R. Co.*, 338 U.S. 263, 266. See also *Krenger* v. *Pennsylvania Railroad Co.*, 174 F. 2d 556, 561 (C.A. 2), certiorari denied, 338 U.S. 866.

5, 15 U.S.C. § 77e). The instant stipulation, on the contrary, commits the customer in advance of any transaction to a waiver of important rights which would accrue to him as the result of the seller's failure to comply with the statute. While the stipulation here in question was exacted by a broker-dealer in connection with the opening of an account, the decision below may well suggest exaction of similar stipulations for arbitration by issuers and underwriters who desire to avoid lawsuits under the companion civil liability provisions of Section 11 of the Act, 15 U.S.C. § 77k, on account of misrepresentations or omissions in registration statements.

As the dissenting judge stated, commercial arbitration has been highly useful in providing a businessman's adjudication of a business dispute; but it would be "vastly unfortunate" if the presale stipulation exacted here "became usable as a device to blunt or break social legislation" (R. 50-51). Yet, it is such a device that the majority below has sanctioned.

CONCLUSION

The decision below renders capable of nullification important rights which Congress intended to afford public investors, and is in conflict with the Securities Act of 1933. It should be reversed.

Respectfully submitted,

ROBERT L. STERN,
Acting Solicitor General.

WILLIAM H. TIMBERS,
General Counsel,

ROGER S. FOSTER,
ALEXANDER COHEN,
Special Counsel,

GEORGE H. JAFFIN,
Attorney,

Securities and Exchange Commission.

October, 1953.

☆U. S. GOVERNMENT PRINTING OFFICE 1953—274528/P.O. 405

APPENDIX

MARGIN AGREEMENT

2M 9 48
FORM 220

HAYDEN, STONE & CO.
25 Broad Street
New York, N. Y.

January 18, 1951 19

Dear Sirs: In consideration of your opening now or in the future or continuing an account or accounts in my name or for me for the purchase or sale of property, I agree with you and your successors as follows, all my relations and dealings with you being subject to this agreement:

The word "property" as used herein shall include shares of stock, certificates of shares of stock, scrip certificates, stock warrants or rights, and bonds, notes, debentures and other evidences of indebtedness whether secured or unsecured and the security therefor, and commodities and contracts for the future delivery of commodities and other securities of every kind and nature, and contracts for property, and all other property usually and customarily dealt in on Exchanges, Boards or Markets or by stock brokerage firms.

All transactions made by you or your agents for me are to be subject to the constitutions, rules, customs and practices of the exchanges or markets where executed and of their respective clearing houses and shall be subject to the provisions of the Securities Exchange Act of 1934 and present and future acts amendatory thereof or supplemental thereto, and to the rules and regulations of the Federal Securities and Exchange Commission and of the Federal Reserve Board insofar as they may be applicable, and shall also be subject to the provisions of the Commodity Exchange Act and present and future acts amendatory thereof or supplemental thereto, and to the rules and regulations of the Secretary of Agriculture insofar as they may be applicable. All orders for the purchase or sale of any property are given by me and executed with the distinct understanding that an actual purchase or sale is intended and that it is my intention and obligation in every case to deliver certificates or commodities to cover any and all of my sales and in the case of purchases to receive and pay for certificates or commodities and that I will do so upon your demand. In case you make a short sale of any property at my direction or in case I fail to deliver to you any property which you have sold at my direction, I authorize you to borrow the property necessary to enable you to make delivery to the purchaser and I agree to be responsible for the cost or loss you may thus incur, or the cost of otherwise obtaining the property if you are unable to borrow it. No settlement of any account for me may be made by me without all property in which my account is short being received by you and all property in which my account is long being paid for in full and the property then delivered, and you and your correspondents are hereby constituted agents of mine for the purpose of consummating all such transactions, and are authorized to make such advances and expend such moneys as may be required in respect thereof. When placing with you any sell order for short account I will designate it as such and hereby authorize you to mark such order as being "short", and when placing with you any order for long account I will designate it as such and hereby authorize you to mark such order as being "long". Any sell order which I shall designate as being for long account will be for securities then owned by me and if such securities are not then deliverable by you from any account of mine, the placing of such order shall constitute a representation by me that I will deliver such securities as soon as I can do so without undue inconvenience or expense.

Any order given you by me shall be binding upon me and my personal representatives until you have actual notice of my death, but my death and notice thereof shall not in any way affect your rights under this agreement to take any action which you could have taken if I had not died.

Subject to the provisions of applicable statutes and regulations thereunder, all property now or hereafter held or purchased by you for me shall be subject to a general lien for the payment of all liabilities of mine to you however and whenever arising, and you are hereby authorized without notice to me whenever you deem it advisable, from time to time to transfer interchangeably between any accounts I have with you any or all of the property so held, and without further notice to me and without regard to whether you have in your possession or subject to your control at the time thereof other property of the same kind and amount, in the usual course of business to pledge, repledge, hypothecate, rehypothecate (either for the amount due you from me or for a greater sum) and lend the same to yourselves as brokers or to others from time to time, separately or together with other property and you shall not be required to deliver to me the same property deposited or received but only property of the same kind and amount.

You may at any time demand that my account or accounts immediately be taken up and paid, and all amounts advanced and other balances due, with interest at the current rate, and all commissions fixed by the regulations and usages of the exchange or market where orders are executed shall be due and payable upon demand. I will at all times maintain margins for said accounts as from time to time required by you.

You may employ sub-brokers and shall be responsible only for reasonable care in their selection and may settle contracts and controversies according to the regulations and customs of the Exchange or Market where the orders are executed. You may deal with members of any Exchange known as specialists or known as odd lot dealers and in the execution of my orders they may act as sub-brokers for me and may also buy or sell the property for themselves as dealers on their own accounts.

Upon my death or failure to comply with any of the provisions hereof, or whenever you deem it necessary for your protection (it being understood that on transactions in securities when, as and if issued you are entitled to protection against your contingent liability pending the issue of the securities to the same extent as in purchases and sales of securities already issued and that you may purchase or sell odd lots on offer or bid without waiting for a round lot transaction) you are hereby authorized and empowered to cancel outstanding orders, sell, assign and deliver all or any part of the property or contracts for property held or carried for me and close out short sales by purchase upon any exchange or market or at any public or private sale at your option, all without demand for margin or notice of purchase or sale, which are expressly waived, and no specific demand or notice shall invalidate this waiver, and after deducting all costs and expenses of purchase or of

Account Name ILKO, Anthony MA

me shall be subject to a general lien for the payment of all liabilities of mine to you wherever and whenever arising, and you are hereby authorized without notice to me whenever you deem it advisable, from time to time to transfer interchangeably between any accounts I have with you any or all of the property so held, and without further notice to me and without regard to whether you have in your possession or subject to your control at the time thereof other property of the same kind and amount, in the usual course of business to pledge, repledge, hypothecate, rehypothecate (either for the amount due you from me or for a greater sum) and lend the same to yourselves as brokers or to others from time to time, separately or together with other property and you shall not be required to deliver to me the same property deposited or received but only property of the same kind and amount.

You may at any time demand that my account or accounts immediately be taken up and paid, and all amounts advanced and other balances due, with interest at the current rate, and all commissions fixed by the regulations and usages of the exchange or market where orders are executed shall be due and payable upon demand. I will at all times maintain margins for said accounts as from time to time required by you.

You may employ sub-brokers and shall be responsible only for reasonable care in their selection and may settle contracts and contraverses according to the regulations and customs of the Exchange or Market where the orders are executed. You may deal with members of any Exchange known as specialists or known as odd lot dealers and in the execution of my orders they may act as sub-brokers for me and may also buy or sell the property for themselves as dealers on their own accounts.

Upon my death or failure to comply with any of the provisions hereof, or whenever you deem it necessary for your protection (it being understood that on transactions in securities when, as and if issued you are entitled to protection against your contingent liability pending the issue of the securities to the same extent as in purchases and sales of securities already issued and that you may purchase or sell odd lots on offer or bid without waiting for a round lot transaction) you are hereby authorized and empowered to cancel outstanding orders, sell, assign and deliver all or any part of the property or contracts for property held or carried for me and close out short sales by purchase upon any exchange or market or at any public or private sale at your option, all without demand for margin or notice of purchase or sale, which are expressly waived, and no specific demand or notice shall invalidate this waiver, and after deducting all costs and expenses of purchase or of sale and delivery, to apply the residue of the proceeds to the payment of my liabilities to you, returning the surplus, if any, to me, and I shall remain liable for any deficiency. At any such sale at public auction or on any exchange you may become purchasers for yourselves or in behalf of anyone else.

I expressly agree that you shall not be bound by any representation or agreement heretofore or hereafter made by any of your employees or agents which in any way purports to affect or diminish your rights under this agreement and that no representation or advice by you or your employees or agents regarding the purchase or sale by me of any property bought or sold on my order or carried or held in any manner for my account shall be the basis of any liability on your part to me.

Whenever any statute shall be enacted, or any regulation made under any statute or by the New York Stock Exchange, which shall be applicable to and affect in any manner or be inconsistent with any of the provisions hereof, the provisions of this agreement so affected shall be deemed modified or superseded, as the case may be, by such statute or regulation and all other provisions of this agreement and the provisions as so modified shall in all respects continue and be in full force and effect.

Whenever in your opinion circumstances require it, you may apply and/or transfer any of or all my equities interchangeably between all my said accounts, without notice to me in the premises, subject always to the rules and regulations under the Commodity Exchange Act.

I hereby ratify all transactions and dealings with property by you previous to the date hereof which would have been authorized by the terms of this agreement had they been subsequent hereto.

You are not to be in any way responsible or liable for any decline in price of property bought on my order, or carried or held in any manner for my account, nor for any rise in price of property sold short on my order.

My address herein below given is correct and shall be my address until I shall give you notification of a change by written notice received by you, and the sending of notices and other communications by you to such address or to such changed address shall be deemed personal delivery thereof to me.

I hereby represent that I am over 21 years of age and that I am not an employee of any exchange or of any corporation of which any exchange owns a majority of the capital stock, or of a member of or any firm registered on any exchange, or of a bank, trust company, insurance company or of any corporation, association, firm or individual engaged in the business of dealing, either as broker or principal, in stocks, bonds, or other securities or any forms of commercial paper, and if at any time during the life of this agreement I become so I will notify you. No one other than myself has or will have an interest in any account governed hereby except as I advise you in writing.

This agreement and its enforcement shall be governed by the laws of the State of New York and its provisions shall be continuous and shall cover individually and collectively all accounts which the undersigned may open or reopen with you, and shall enure to the benefit of your present firm, and any successor firm or firms, irrespective of any changes or changes at any time in the personnel thereof, for any cause whatsoever, and of the assigns of your present firm or any successor firm, and shall be binding upon the undersigned, and/or the estate, executors, administrators and assigns of the undersigned.

Any controversy arising between us under this contract shall be determined by arbitration pursuant to the Arbitration Law of the State of New York, and under the rules of either the Arbitration Committee of the Chamber of Commerce of the State of New York, or of the American Arbitration Association, or of the Arbitration Committee of the New York Stock Exchange or such other Exchange as may have jurisdiction over the matter in dispute, as I may elect. Any arbitration hereunder shall be before at least three arbitrators.

Signature Anthony Wilko

Address { 36 Pelham Parkway West / NO. AND STREET
New Rochelle, N.Y. / CITY OR TOWN

McCabe

ACCEPTED

HAYDEN, STONE & CO.

By C W Gillies

at NEW YORK, N. Y. [illegible] 19 [illegible]

On _____ 19____

NEW YORK
MARGIN AGREEMENT

Name
Anthony

WILKO, Anthony

49

LIBRARY
SUPREME COURT, U.S.

Office - Supreme Court, U. S.
FILED
MAY 21 1953
HAROLD B. WILLEY, Clerk

IN THE

Supreme Court of the United States

October Term, ~~1952~~ 1953

No. ~~715~~ 39

ANTHONY WILKO,

Petitioner,

against

JOSEPH E. SWAN, *et al.,*
individually and doing business under the firm name and style of Hayden, Stone & Co.,

Defendants-Respondents,

and

HAVEN B. PAGE,

Defendant.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR RESPONDENTS JOSEPH E. SWAN, ET AL. IN OPPOSITION

LEONARD P. MOORE,
25 Broadway,
New York 4, New York,
Attorney for Respondents.

EDWIN C. HOYT, JR.,
FRANCIS E. KOCH,
ALAN S. KULLER,
of Counsel.

INDEX

	PAGE
OPINIONS BELOW	1
JURISDICTION	2
QUESTION PRESENTED	2
STATUTES INVOLVED	2
STATEMENT OF THE CASE	3
ARGUMENT	5
I. The case is not ripe for review	6
II. The decision below was correct	8
III. There is no conflict of decision	15
CONCLUSION	16
APPENDIX A	17

TABLE OF AUTHORITIES

CASES

Agostini Bros. Bldg. Corp. v. United States, 142 F. 2d 854 (4 Cir. 1944)	10, 11
Brown v. Allen, 344 U. S. 443 (1953)	6
Campbell v. American Fabrics Co., 168 F. 2d 959 (2 Cir. 1948)	13

PAGE

Columbian Fuel Corp. v. United Fuel Gas Co., 72 F. Supp. 843 (S. D. W. Va. 1947), aff'd, 165 F. 2d 746 (4 Cir. 1948) 13

Czarnikow v. Roth, Schmidt & Co., [1922] 2 K. B. 478 13

Donahue v. Susquehanna Collieries Co., 138 F. 2d 3 (3 Cir. 1943) 10, 11

Evans v. Hudson Coal Co., 165 F. 2d 970 (3 Cir. 1948) 13

Hamilton-Brown Shoe Co. v. Wolf Brothers & Co., 240 U. S. 251 (1916) 7

House v. Mayo, 324 U. S. 42 (1945) 6

Jager v. Tolme, [1916] 1 K. B. 939 13

In re Konvitz (McCosker-Hershfield Cardiac Home, Inc.), 129 N. Y. L. J. 1639, col. 8 (Sup. Ct. May 15, 1953) 17

Lipschutz v. Gutwirth, 304 N. Y. 58, 106 N. E. 2d 8 (1952) 12

Murray Oil Products Co. v. Mitsui & Co., 146 F. 2d 381 (2d Cir. 1944) 11

Petrol Corporation v. Groupement d'Achat des Carburants, 84 F. Supp. 446 (S. D. N. Y. 1949) 12

Sargant v. Monroe, 268 App. Div. 123, 49 N. Y. S 2d 546 (1st Dep't 1944) 13

Sargant v. Monroe, 268 App. Div. 755 (1st Dep't 1944) 13

Matter of Springs Cotton Mills (Buster Boy Suit Co.), 275 App. Div. 196, 88 N. Y. S. 2d 295 (1st Dep't), aff'd, 300 N. Y. 586, 89 N. E. 2d 877 (1949) 14

PAGE

Stathatos v. Arnold Bernstein S. S. Corp., 202 F. 2d 525 (2 Cir. 1953) 7, 12

Stotesbury v. Turner, [1943] K. B. 370 13

Tarello v. John A. Johnson Contracting Corp., 50 N. Y. S. 2d 212 (not officially reported) (Sup. Ct.), aff'd, 268 App. Div. 893, 51 N. Y. S. 2d 87, leave to appeal denied, 268 App. Div. 903, 51 N. Y. S. 2d 640 (1st Dep't 1944), 294 N. Y. 646, 58 N. E. 2d 523 (1945) 14

Toledo S. S. Co. v. Zenith Transp. Co., 184 Fed. 391 (6 Cir. 1911) 14

Watkins v. Hudson Coal Co., 151 F. 2d 311 (3 Cir. 1945), cert. denied, 327 U. S. 777 (1946) 10, 14

STATUTES

Fair Labor Standards Act of 1938, 52 Stat. 1060, 29 U. S. C. §§201-219 10

Federal Arbitration Act, 61 Stat. 669, 9 U. S. C. §§1-14

Sec. 3, 61 Stat. 670, 9 U. S. C. §3 4

Sec. 10, 61 Stat. 672, 9 U. S. C. §10 ..... 2, 5, 12

Miller Act, 49 Stat. 793, 40 U. S. C. §§270a-270d 10

Sec. 2, 49 Stat. 794, 40 U. S. C. §270b 11

Securities Act of 1933, 48 Stat. 74, 15 U. S. C. §§77a-77aa

Sec. 12(2), 48 Stat. 84, 15 U. S. C. §771(2) .. 2, 3, 5, 7, 8, 10, 11, 12, 15

Sec. 14, 48 Stat. 84, 15 U. S. C. §77n 2, 10, 15

Other Authorities

PAGE

Commercial Arbitration Rules of the American Arbitration Association (as amended and in effect January 1, 1952)

Rules 11-19 13

Rule 11 13

Rule 18 13

Robertson and Kirkham, Jurisdiction of the Supreme Court of the United States (1951) 7

Sturges, Address before the Association of the Bar of the City of New York, (74 Reports, Association of the Bar, 1941) 14

IN THE

Supreme Court of the United States

October Term, 1952

No. 715

ANTHONY WILKO,

Petitioner,

against

JOSEPH E. SWAN, *et al.*,

individually and doing business under the firm name and style of Hayden, Stone & Co.,

Defendants-Respondents,

and

HAVEN B. PAGE,

Defendant.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR RESPONDENTS JOSEPH E. SWAN, ET AL. IN OPPOSITION

Opinions Below

The opinion of the United States District Court (23-32)* is reported in 107 F. Supp. 75. The opinion of the

---

* Unless otherwise stated, references in parentheses are to pages of the record.

United States Court of Appeals for the Second Circuit (40-52) is reported in 201 F. 2d 439.

Jurisdiction

The jurisdictional requisites are adequately set forth in the petition and the brief of the *amicus curiae*.

Question Presented

In a civil action for damages allegedly suffered because of misrepresentations in the sale of securities, brought under section 12(2) of the Securities Act of 1933, 15 U. S. C. §77*l*(2), was it error, because of section 14 of the Securities Act, 15 U. S. C. §77n, for the Court of Appeals to direct the enforcement of an agreement between the purchaser and seller of the securities for arbitration of the controversy, where the arbitration agreement was subject to the Securities Act, and the failure of the arbitrators to decide in accordance with section 12(2) of the Securities Act would be grounds for vacating the arbitration award pursuant to section 10 of the Federal Arbitration Act, 9 U. S. C. §10?

It is respectfully submitted that petitioner's questions present issues which are not in the case at all and that the questions presented by petitioner and *amicus* are based upon incorrect assumptions as to the procedure to be followed by arbitrators.

Statutes Involved

The pertinent provisions of the Federal Arbitration Act and the Securities Act of 1933 are set forth in the brief of the *amicus curiae* at pp. 3-5.

Statement of the Case

Petitioner is a citizen of the state of New York (2). Respondents are a partnership doing business in New York under the name Hayden, Stone & Co. (7). They are stockbrokers and dealers in securities and with reference to the transactions herein are subject to the Securities Act of 1933.

Petitioner brought suit against respondents* for damages of $3,888.88 under section 12(2) of the Securities Act of 1933. His complaint (2-4) alleges in substance that on or about January 17, 1951, respondents sold to petitioner 1,600 shares of the common stock of Air Associates, Incorporated, a New Jersey corporation, and that petitioner paid respondent $29,517.54 therefor. The complaint further alleges that said sale was made by means of certain instrumentalities of transportation and communication in interstate commerce and that it

> "was made by means of communications by the defendants to the plaintiff which were and, which included untrue statements of material facts and omitted to state material facts necessary in order to make the statements made in the light of the circumstances under which they were made, not misleading" (Par. FIFTH; 3).

The complaint further alleges that petitioner did not know that the alleged statements were untrue at the time of his purchase of the stock and petitioner sold the stock on or about February 2 and 3, 1951 (less than three weeks after the purchase) for $25,628.61, at a loss of $3,888.88.

---

* Petitioner joined as a defendant Haven B. Page, who is not involved in any of the questions presented by the petition herein.

The relationship between petitioner and respondent was controlled by the terms and conditions of Margin Agreements duly executed by petitioner dated May 2, 1950 and January 18, 1951 (8-9). The agreement of May 2, 1950 opened a joint account on behalf of Anthony Wilko and Mary Wilko (16). The agreement of January 18, 1951 opened a separate account in the name of Anthony Wilko alone (22). The agreements were otherwise identical (43 n. 4). The transaction which is the subject of the complaint in this action took place on January 17, 1951 and was on behalf of the joint account. The last paragraph of these agreements, which was directly above the place for petitioner's signature and was in the same size type as the rest of the agreement, provided:

> "Any controversy arising between us under this contract shall be determined by arbitration pursuant to the Arbitration Law of the State of New York, and under the rules of either the Arbitration Committee of the Chamber of Commerce of the State of York, or of the American Arbitration Association, or of the Arbitration Committee of the New York Stock Exchange or such other Exchange as may have jurisdiction over the matter in dispute, as I may elect. Any arbitration hereunder shall be before at least three arbitrators" (16, 22).

The Court of Appeals noted that petitioner made no claim of "fraud or coercion in procuring his signature to the agreement" (44).

Before answering the complaint respondents moved (5-6), pursuant to section 3 of the Federal Arbitration Act, 9 U. S. C. §3, for an order staying all proceedings in the

action until an arbitration had been had in accordance with the arbitration provision of the margin agreement quoted above. Respondents' motion was made upon the complaint, the affidavit of Sherman M. Bijur, a partner of Hayden, Stone & Co. (7-10), and copies of the margin agreements involved (11-22). These constituted the whole record; petitioner submitted no opposing affidavit (43).

The District Court denied the motion, because it did not "feel that arbitration of the issues at bar is consistent with the policy and language as expressed by Congress in the Securities Act" (32).

The Court of Appeals for the Second Circuit reversed (Judge Clark dissenting). Chief Judge Swan wrote an opinion, in which Judge Chase concurred, holding that "we do not find in the purpose or in the language of the statute, any policy argument strong enough to override the policy of the Arbitration Act" (49). The court also held that the margin agreement was subject to the Securities Act of 1933 and "consequently the arbitrators are bound to decide in accordance with the provisions of section 12(2)" and that "Failure to do so would . . . constitute grounds for vacating the award pursuant to section 10 of the Federal Arbitration Act, 9 U. S. C. A. §10" (48, 49).

To review this interlocutory order, petitioner filed this petition for certiorari.

ARGUMENT

The decision below is a sound and carefully reasoned accommodation of the purposes and policies of two federal

statutes. Without attempting to follow the procedure directed by the Court of Appeals, petitioner, joined by the Securities and Exchange Commission, urges this court to consider and reject it because of speculative fears of what might otherwise happen.

Respondents believe these fears are groundless and that the Court of Appeals gave full effect to both the Securities Act and the Federal Arbitration Act.

Respondents further believe that the procedure directed by the Court of Appeals will result in a prompt, fair and inexpensive trial on the merits and that review by this court of the interlocutory decision of the Court of Appeals before final judgment is entered after completion of the proceedings below would be premature.

I

The Case Is Not Ripe for Review

The decision below was interlocutory (43), and did not in any way determine the right of petitioner to recover the damages alleged in the complaint. Rather, the decision directed that the controversy be tried in the forum agreed upon by the parties, *i.e.*, arbitration. If this court denies certiorari at this time, petitioner may speedily obtain a trial and decision before arbitrators, and if he is successful, the questions now presented will be moot. If he is unsuccessful on the merits, petitioner may then seek review by this court, for the denial of certiorari is not, of course, equivalent to an affirmance of the decision below, *Brown* v. *Allen*, 344 U. S. 443, 488, 491 (1953); *House* v. *Mayo*, 324

U. S. 42, 48 (1945), and on certiorari from the final judgment this court may review the interlocutory order directing arbitration.* *Hamilton-Brown Shoe Co.* v. *Wolf Brothers & Co.*, 240 U. S. 251, 258-9 (1916); Robertson and Kirkham, *Jurisdiction of the Supreme Court of the United States* 233-34 (1951). Cf. *Stathatos* v. *Arnold Bernstein S. S. Corp.*, 202 F. 2d 525, 528 (2 Cir. 1953).

Under the circumstances of this case it is especially preferable to postpone review until the proceedings ripen into a final judgment after arbitration.

The Court of Appeals held that the purposes and policies of both of those acts could best be secured by enforcing the arbitration agreement and by requiring the arbitrators to decide in accordance with the provisions of section 12(2) of the Securities Act (49).

Petitioner and the SEC, as *amicus curiae*, maintain that the procedure directed by the Court of Appeals will not accommodate these two statutory schemes, but will subvert the purposes and policies of the Securities Act. Thus, petitioner contends that the decision below constitutes a "long step backward in the enforcement of federal statutes; back to the days before 1933 when the 'lambs' were shorn regularly and continuously by the 'wolves' of Wall Street" (Petition, p. 17). The *amicus* alleges that "arbitration cannot assure the customer of the equivalent of his statu-

* Because of the calendar congestion both in the state courts and the federal court in New York City (47), this controversy may be arbitrated, the arbitration award reviewed by the District Court and Court of Appeals, and certiorari thereafter sought, all before there would be any possibility of the case's being reached for trial in ordinary course, if there were no arbitration provision.

tory rights" (Brief, p. 10) and speculates at length as to the possible pitfalls in the arbitration procedure directed by the decision below.

Actually, both the petitioner and *amicus* call upon this court to make a guess that arbitration under the conditions specified by the Court of Appeals will not safeguard the rights granted petitioner by section 12(2) of the Securities Act. But why guess at this time, when it is possible actually to see the arbitration procedure in action and then, if necessary, decide as to its propriety?

Granted all that petitioner and *amicus* say about the importance of the questions presented, it then becomes imperative that, insofar as possible, the ultimate determination of the case rests upon facts actually developed rather than fears and conjectures as to what may happen but has not happened.

II

The Decision Below Was Correct

The basic issue decided by the Court of Appeals was the enforceability of an agreement to arbitrate a controversy subject to the Securities Act. Before deciding this basic question, the Court of Appeals disposed of some preliminary problems peculiar to this case some of which petitioner evidently desires to resurrect in this court.

First, the Court of Appeals held that "In the absence of any opposing affidavit by the plaintiff charging fraud or coercion in procuring his signature to the agreement . . . we must assume that the plaintiff voluntarily entered

into the agreement and fully understood its terms" (43-44; cf. Petition, p. 5, question 1).

Second, the Court of Appeals held that paragraph three of the margin agreement which provides that all transactions "shall be subject to the provisions of the Securities Exchange Act of 1934 and *present* and future acts amendatory thereto," should be construed to include the Securities Act of 1933 (emphasis supplied), and that in any event the sale transaction would necessarily be subject to that Act (45-46). Neither petitioner nor *amicus* challenges this holding.

Third, the Court of Appeals held that the presence in the margin agreement of a concededly invalid provision purporting to exempt respondents from liability based on representations of its agents (14, 20) did "not vitiate the entire agreement" (45). This holding is not directly challenged. However, in spite of the fact that the Court of Appeals held that "no question as to [the exculpatory provision] will be submitted to the arbitrators" (48), *amicus* now contends, "There is no assurance, moreover, that lay arbitrators would not be influenced in some degree by the exculpatory provision of the margin agreement which is concededly invalid" (Brief, p. 18). This is but a revival of the ancient and now supposedly outmoded distrust of arbitration which may lie at the root of petitioner's and *amicus'* objections to the decision of the Court of Appeals.

With these three preliminary considerations disposed of, none of which requires further review by this court, the Court of Appeals turned to the basic issue in this case —the enforceability of the agreement to arbitrate.

The Court of Appeals noted that the Securities Act did not expressly prohibit referring a controversy subject to that Act to arbitration (46).* Therefore, arbitration would be barred by section 14 of the Securities Act, 15 U. S. C. §77n, only to the extent that arbitration conflicted with the "three things" (46) done by section 12(2) of the Securities Act, and the Court of Appeals correctly held there was no such conflict (46-49).

1. Section 12(2) "gives the purchaser a statutory cause of action against the seller if the purchase was induced by the seller's false or misleading statements" (46). The *amicus* concedes (Brief, p. 16 n. 9), and petitioner does not challenge, the correctness of the holding below that merely because "the suit asserts a statutory cause of action is not alone enough to preclude arbitration of the controversy" (46). Accord, *Watkins* v. *Hudson Coal Co.*, 151 F. 2d 311 (3 Cir. 1945), cert. denied, 327 U. S. 777 (1946); *Agostini Bros. Bldg. Corp.* v. *United States*, 142 F. 2d 854 (4 Cir. 1944); *Donahue* v. *Susquehanna Collieries Co.*, 138 F. 2d 3 (3 Cir. 1943).

2. Section 12(2) provides that the purchaser "may sue in any court of competent jurisdiction" (46). The Court of Appeals held that this provision, like similar provisions in the Miller Act, 40 U. S. C. §§270a-270d, and of the Fair

---

*Cf. *Donahue* v. *Susquehanna Collieries Co.*, 138 F. 2d 3, 6 (3 Cir. 1943) ("Is there anything about the Fair Labor Standards Act which removes claims under its terms from the arbitration clause? We may concede that Congress could have done so had it wished. It could have provided that any claim under the Act was to be enforced by lawsuit only, notwithstanding any agreement between parties for any other method of settlement. There is no such express language.").

Labor Standards Act, 29 U. S. C. §§201-219, was not intended to limit the venue in which the controversy would be resolved, and that it did not bar arbitration which is "merely a form of trial, to be adopted in the action itself, in place of a trial at common law." *Murray Oil Products Co.* v. *Mitsui & Co.*, 146 F. 2d 381, 383 (2 Cir. 1944). Accord, *Agostini Bros. Bldg. Corp.* v. *United States*, 142 F. 2d 854 (4 Cir. 1944);* *Donahue* v. *Susquehanna Collieries Co.*, 138 F. 2d 3, 6 (3 Cir. 1943) ("the effect of this provision is to allow a suitor to proceed in federal court regardless of citizenship of the litigants and amount involved or to sue in a state court at his convenience").

Under the position taken by petitioner and *amicus*, a purchaser would be obligated to sue in every case, even though "There is good reason why he may prefer to seek enforcement of his statutory right to damages through the speedy remedy of arbitration rather than by the long delayed remedy of trial in the courts" (47).

3. Section 12(2) changes the common law rule as to burden of proof—"*i.e.*, if the buyer proves that he bought in reliance on a false statement by the seller or one that was misleading because of the omission to state a material fact, the seller must prove that he did not know, and in

---

* This case arose under the Miller Act which provided: "(b) *Every suit instituted under this section shall* be brought in the name of the United States for the use of the person suing, in the United States District Court for any district in which the contract was to be performed and executed *and not elsewhere*, irrespective of the amount in controversy . . ." (40 U. S. C. §270b) [Emphasis supplied].

Despite this apparent command, the stay pending arbitration was granted.

the exercise of reasonable care could not have known, that his statement was untrue or misleading" (46).

The Court of Appeals held that "the arbitrators are bound to decide in accordance with the provisions of section 12(2)," including the burden of proof provision, and that "Failure to do so would . . . constitute grounds for vacating the award pursuant to section 10 of the Federal Arbitration Act, 9 U. S. C. A. §10" (49).

Petitioner and *amicus* strenuously attack this holding, going so far as to challenge the integrity and good faith of as yet unchosen arbitrators, thus again revealing their unreasoned distrust of arbitration as a means of obtaining justice. Respondents have no doubt that honest arbitrators prepared to heed the directions of the courts are available. And, of course, the District Court would not confirm an award where the arbitrators are shown to have been actually or potentially biased. See *Stathatos* v. *Arnold Bernstein S. S. Corp.*, 202 F. 2d 525, 526 (2 Cir. 1953); *Petrol Corporation* v. *Groupement d'Achat des Carburants*, 84 F. Supp. 446, 447 (S. D. N. Y. 1949); cf. *Lipschutz* v. *Gutwirth*, 304 N. Y. 58, 106 N. E. 2d 8 (1952). See also Appendix A, *infra* p. 17.

Amicus' contention (Brief, p. 18) joined in by petitioner (Petition, p. 9), that the arbitrators would be "selected by the regulated industry" and would be "laymen who would hear and decide the claim without reference to technical rules of law and procedure" is completely unsupported in fact. The arbitration clause (16, 22) itself gives petitioner (not respondents) the right to choose which rules of arbitration shall be used, including among them the

rules of the American Arbitration Association. That association maintains a panel of arbitrators, many of whom are lawyers, and the rules provide a method of selection of arbitrators from that panel by the parties to the dispute. Commercial Arbitration Rules of the American Arbitration Association, Rules 11-19 (as amended and in effect January 1, 1952).*

There is nothing inherently impossible about arbitrators following legal rules. Indeed, in England the arbitrators must decide "according to the legal rights of the parties" (48 n. 9). *Jager* v. *Tolme*, [1916] 1 K. B. 939, 953; *Czarnikow* v. *Roth, Schmidt & Co.*, [1922] 2 K. B. 478, 484; *Stotesbury* v. *Turner*, [1943] K. B. 370. For the record in an actual English arbitration, see records on appeal in *Sargant* v. *Monroe*, 268 App. Div. 123, 755, 49 N. Y. S. 2d 546 (1st Dep't 1944). Respondents know of no case in this country which holds that arbitrators may not be required, by the terms of the submission, to follow legal standards. On the contrary, there are many instances of arbitrators being required to decide in accordance with a specific statute or in accordance with a standard set forth in the submission agreement. *Campbell* v. *American Fabrics Co.*, 168 F. 2d 959, 962 (2 Cir. 1948); *Evans* v. *Hudson Coal Co.*, 165 F. 2d 970, 974 (3 Cir. 1948); *Columbian Fuel Corporation* v. *United Fuel Gas Co.*, 72 F. Supp. 843, 844-45 (S. D. W. Va. 1947), aff'd, 165 F. 2d 746 (4 Cir. 1948); *Watkins* v.

---

* Rule 11 provides that "No person shall serve as an Arbitrator in any arbitration if he has any financial or personal interest in the result of the arbitration, unless the petitioner, in writing, waive such disqualification."

Rule 18 provides that "the prospective arbitrator is requested to disclose any circumstances likely to create a presumption of bias or which he believes might disqualify him as an impartial arbitrator."

Hudson Coal Co., 151 F. 2d 311, 313, 321 (3 Cir. 1945), cert. denied, 327 U. S. 777 (1946); *Toledo S. S. Co.* v. *Zenith Transp. Co.*, 184 Fed. 391, 392, 395 (6 Cir. 1911)*.

The New York courts consider it a matter of course that arbitrators must decide in accordance with law if the submission so provides. See *Matter of Springs Cotton Mills (Buster Boy Suit Co.)*, 275 App. Div. 196, 200, 88 N. Y. S. 2d 295 (1st Dep't), aff'd, 300 N. Y. 586, 89 N. E. 2d 877 (1949); cf. *Tarello* v. *John A. Johnson Contracting Corporation*, 50 N. Y. S. 2d 212 (not officially reported) (Sup. Ct.), aff'd, 268 App. Div. 893, 51 N. Y. S. 2d 87, leave to appeal denied, 268 App. Div. 903, 51 N. Y. S. 2d 640 (1st Dep't 1944), 294 N. Y. 646, 58 N. E. 2d 523 (1945).

Are the parties to be denied the benefits of their contractual agreement merely because the petitioner and *amicus* feel that the arbitrators will not follow the law? If so, is this really more than a concession that the courts are helpless in the situation? Such a concession is wholly unnecessary because section 10 of the Federal Arbitration Act affords specific protection against this possibility.

As the Court of Appeals pointed out (48), the petitioner and *amicus* relied primarily on the burden of proof provision of section 12(2) as creating a conflict with the Federal

---

* ". . . whether the arbitrator shall hear the case according to rules of the law of evidence and/or according to substantive law, depends upon the agreement of the parties; they may agree that one or more of those rules shall apply." Dean Wesley A. Sturges, address before the Association of the Bar of the City of New York (74 Reports, Association of the Bar, 1941.)

Arbitration Act which must be resolved in favor of the Securities Act because of section 14 of that Act. But this reliance is based entirely on their unfounded assertions that the arbitrators will refuse to obey the mandate of the courts to decide in accordance with the Securities Act, and that the courts will be powerless to prevent such conduct by the arbitrators.

In the light of the clearly correct holdings of the Court of Appeals that the arbitrators are bound to decide in accordance with section 12(2) of the Securities Act, and that failure to do so would require vacating the award, the main objections to the decision below evaporate. In any event, if the dire prophecies of petitioner and *amicus* prove correct, this court will have an adequate opportunity, after the entry of final judgment upon the award of the arbitrators, to consider the question.

III

There Is No Conflict of Decision

Petitioner's contention (Petition, pp. 14-15) that the decision below conflicts with five decisions of various Courts of Appeals is unsound. None of the cases cited deals with the impact of the Securities Act of 1933 upon the Federal Arbitration Act or with the power of district judges to require arbitrators to follow applicable law. The brief of the *amicus*, which is thoroughly conversant with cases arising under the Securities Act and related acts, does not allege any conflict of decision.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

LEONARD P. MOORE,
25 Broadway,
New York 4, New York,
Attorney for Respondents.

EDWIN C. HOYT, JR.,
FRANCIS E. KOCH,
ALAN S. KULLER,
of Counsel.

APPENDIX A

A very recent instance of the exercise by a New York court of its powers to secure the selection of arbitrators free from bias is found in the following decision of Mr. Justice Steuer, sitting in New York County, which is a part of the Southern District of New York where this controversy arose, in *In re Konvitz (McCosker-Hershfield Cardiac Home, Inc.)*, 29 N. Y. L. J. 1639, col. 8 (not officially reported) (Sup. Ct. May 15, 1953):

> "This is a petition to have the court appoint an arbitrator. Petitioner had a contract of employment with respondent, a charitable organization. The contract provided for arbitration of disputes by a board of three arbitrators, one to be selected by each of the parties and the third by the two previously so selected. The parties selected their arbitrators, Petitioner objected to respondent's arbitrator on the ground that he would be biased as he is one of the trustees of respondent. Respondent refused to withdraw its choice or make any other. Its position is that the contract places no restriction on the selection of arbitrators and that the matter will be eventually determined by the third arbitrator. Respondent further points out that for this reason it made no objection to petitioner's arbitrator who would also be disqualified as he is a plaintiff in a current litigation against respondent. Respondent is wrong. Arbitrators are acting judges, not only the third one, but all of them. An arbitration should represent the honest conclusion, not necessarily unanimous, of the three—not the ability of either acting as an advocate to convince the third. By the steps taken respondent has put itself in the position of not being able to

select an arbitrator of its choice and having to accept a biased arbitrator. Despite the fact that the situation is of its own making relief will be tendered. If respondent on or before May 18, 1953, desires to nominate another arbitrator it may do so. Before the same date it may object to petitioner's arbitrator. If it still desires to stand on the position it has taken an arbitrator will be appointed for it. Final determination will be held in abeyance until further advice from the parties."

LIBRARY
SUPREME COURT, U.S.

Office - Supreme Court, U. S.
FILED
OCT 15 1953
HAROLD B. WILLEY, Clerk

IN THE

Supreme Court of the United States

October Term, 1953

No. 39

ANTHONY WILKO,

Petitioner,

against

JOSEPH E. SWAN, *et al.*, individually and doing business under the firm name and style of HAYDEN, STONE & Co.,

Defendants-Respondents,

and

HAVEN B. PAGE,

Defendant.

BRIEF FOR RESPONDENTS JOSEPH E. SWAN, *ET AL.*

HORACE G. HITCHCOCK,
25 Broadway,
New York 4, N. Y.,
Attorney for Defendants-Respondents.

RALPH D. RAY,
FRANCIS E. KOCH,
Of Counsel.

INDEX

PAGE

Opinions Below 1

Jurisdiction 2

Questions Presented 2

Statutes Involved 2

Statement of the Case 4

Summary of Argument 6

Point I—The Provisions and Policy of the Securities Act of 1933 Do Not Forbid Arbitration as a Mode of Settling Disputes Arising from an Alleged Violation of Section 12(2) Thereof 12

Conclusion 34

TABLE OF AUTHORITIES

Cases

A. C. Frost & Co. v. Coeur d'Alene Mines Corp., 312 U. S. 38 (1941) 7

Agostini Bros. Building Corp. v. United States, 142 F. 2d 854 (4th Cir. 1944) 22

The Anaconda v. American Sugar Refining Co., 322 U. S. 42 (1944) 20

Barnes v. Youngs, [1898] 1 Ch. 414 28

PAGE

Boyd v. Grand Trunk Western Railroad Co., 338 U. S. 263 (1949) 23

Brooklyn Savings Bank v. O'Neil, 324 U. S. 697 (1945) 24

Campbell v. American Fabrics Co., 168 F. 2d 959 (2d Cir. 1948) 29

Cavicchi v. Mohawk Manufacturing Co., 308 U. S. 522 (1939) 19, 32

Application of Cohen, 183 Misc. 1034, 52 N. Y. S. 2d 671 (Sup. Ct. 1944), aff'd, 269 App. Div. 663, 53 N. Y. S. 2d 467 (1st Dep't 1945), leave to appeal denied, 269 App. Div. 690, 54 N. Y. S. 2d 389, 294 N. Y. 640, 61 N. E. 2d 459 (1945) 33

Columbian Fuel Corporation v. United Fuel Gas Co., 72 F. Supp. 843 (S. D. W. Va. 1947), aff'd, 165 F. 2d 746 (4th Cir. 1948) 29

Czarnikow v. Roth, Schmidt & Co., [1922] 2 K. B. 478 (C. A.) 26, 27

Application of Diamond, 80 N. Y. S. 2d 465 (not officially reported) (Sup. Ct.), aff'd, 274 App. Div. 762, 79 N. Y. S. 2d 924 (1st Dep't 1948) 33

Donahue v. Susquehanna Collieries Co., 138 F. 2d 3 (3d Cir. 1943) 21

Evans v. Hudson Coal Co., 165 F. 2d 970 (3d Cir. 1948) 29

Green v. Howell, [1910] 1 Ch. 495 (C. A.) 27

Hill v. Hill, 199 Misc. 1035, 104 N. Y. S. 2d 755 (Sup. Ct. 1951) 33

Jager v. Tolme & Runge, [1916] 1 K. B. 939 26

PAGE

Matter of Kingswood Management Corp. (Salzman), 272 App. Div. 328, 70 N. Y. S. 2d 692 (1st Dep't 1947) 32

Kulukundis Shipping Co. v. Amtorg Trading Corp., 126 F. 2d 978 (2d Cir. 1942) 7, 24

Lipschutz v. Gutwirth, 304 N. Y. 58, 106 N. E. 2d 8 (1952) 26

Matter of Mohawk Manufacturing Co. v. Cavicchi, 281 N. Y. 629, 22 N. E. 2d 179 (1939) 19

Murray Oil Products Co. v. Mitsui & Co., 146 F. 2d 381 (2d Cir. 1944) 17

Petrol Corporation v. Groupement d'Achat des Carburants, 84 F. Supp. 446 (S. D. N. Y. 1949) 26

The Quarrington Court, 102 F. 2d 916 (2d Cir.), cert. denied sub nom. Court Line, Ltd. v. Isthmian S. S. Co., 307 U. S. 645 (1939) 33

Red Cross Line v. Atlantic Fruit Co., 264 U. S. 109 (1924) 19

Matter of Springs Cotton Mills (Buster Boy Suit Co.), 275 App. Div. 196, 88 N. Y. S. 2d 295 (1st Dep't), aff'd, 300 N. Y. 586, 89 N. E. 2d 877 (1949) 29

Stathatos v. Arnold Bernstein S. S. Corp., 202 F. 2d 525 (2d Cir. 1953) 26

Stotesbury v. Turner, [1943] K. B. 370 26

Swislocki v. Spiewak, 273 App. Div. 768, 75 N. Y. S. 2d 147 (1st Dep't 1947) 33

Tarello v. John A. Johnson Contracting Corporation, 50 N. Y. S. 2d 212 (not officially reported) (Sup. Ct.), aff'd, 268 App. Div. 893, 51 N. Y. S. 2d 87, leave to

PAGE

appeal denied, 268 App. Div. 903, 51 N. Y. S. 2d 640 (1st Dep't 1944), 294 N. Y. 646, 58 N. E. 2d 523 (1945) 29

Toledo S. S. Co. v. Zenith Transp. Co., 184 Fed. 391 (6th Cir. 1911) 29

United States Alkali Exports Ass'n v. United States, 325 U. S. 196 (1945) 12

United States v. Borden Co., 308 U. S. 188 (1939) ... 12

Wallis v. Hirsch, 26 L. J. C. P. (N. S.) 72, 140 Eng. Rep. 131 (1856) 27

Watkins v. Hudson Coal Co., 151 F. 2d 311 (3d Cir. 1945), cert. denied, 327 U. S. 777 (1946) 23, 29

Workman v. Belfast Harbour Comm'rs, [1889] 2 Ir. R. 234 (Q. B. Div.) 27

Zip Mfg. Co. v. Pep Mfg. Co., 44 F. 2d 184 (D. Del. 1930) 20, 32

STATUTES

Fair Labor Standards Act of 1938, 52 Stat. 1060, 29 U. S. C. §§201-219 21

Sec. 16, 52 Stat. 1069, 29 U. S. C. §216 23

Federal Arbitration Act, 61 Stat. 669, 9 U. S. C. §§1-14

Sec. 1, 61 Stat. 670, 9 U. S. C. §1 ..... 2, 3, 7, 31

Sec. 2, 61 Stat. 670, 9 U. S. C. §2 ..... 2, 3, 7, 10, 11, 31

Sec. 3, 61 Stat. 670, 9 U. S. C. §3 ..... 2, 5, 7, 17, 21, 31

Sec. 8, 61 Stat. 672, 9 U. S. C. §8 20

Sec. 10, 61 Stat. 672, 9 U. S. C. §10 ..... 2, 6, 9

PAGE

Federal Emergency Price Control Act of 1942, 56 Stat. 23, 50 U. S. C. App. §§901 et seq. 32

Federal Employers' Liability Act, 35 Stat. 65, 45 U. S. C. §§51-60

Sec. 5, 35 Stat. 66, 45 U. S. C. §55 24

Miller Act, 49 Stat. 793, 40 U. S. C. §§270a-270d 22

Sec. 2(b), 49 Stat. 794, 40 U. S. C. §270b(b) 23

Securities Act of 1933, 48 Stat. 74, 15 U. S. C. §§77a-77aa

Sec. 6, 48 Stat. 78, 15 U. S. C. §77f 15

Sec. 7, 48 Stat. 78, 15 U. S. C. §77g 15

Sec. 8, 48 Stat. 79, 15 U. S. C. §77h 15

Sec. 10, 48 Stat. 81, 15 U. S. C. §77j 15

Sec. 12(2), 48 Stat. 84, 15 U. S. C. §77*l*(2) ..2, 4, 6, 12, 15, 18, 32

Sec. 14, 48 Stat. 84, 15 U. S. C. §77n 8, 16

28 U. S. C. §1254, 62 Stat. 928 2

28 U. S. C. §1338, 62 Stat. 931 19

OTHER AUTHORITIES

H. R. Rep. No. 96, 68th Cong., 1st Sess. (1924) 14

H. R. Rep. No. 85, 73d Cong., 1st Sess. (1933) 12

Note, *Predictability of Result in Commercial Arbitration*, 61 Harv. L. Rev. 1022 (1948) 25, 26, 30

PAGE

Robb, *Arbitration Procedure Compared with Court Litigation in Patent Controversies*, 17 Law and Contemp. Prob. 679 (1952) 20

Sen. Rep. No. 536, 68th Cong., 1st Sess. (1924) 15

Sen. Rep. No. 1455, 73d Cong., 2d Sess. (1934) 31

Sturges, Address before the Association of the Bar of the City of New York, 74 Reports, Association of the Bar, 1941 29

IN THE

Supreme Court of the United States

October Term, 1953

No. 39

ANTHONY WILKO,

Petitioner,

against

JOSEPH E. SWAN, *et al.*, individually and doing business under the firm name and style of Hayden, Stone & Co.,

Defendants-Respondents,

and

HAVEN B. PAGE,

Defendant.

BRIEF FOR RESPONDENTS JOSEPH E. SWAN, *ET AL.*

Opinions Below

The opinion of the United States District Court (23-32)* is reported in 107 F. Supp. 75. The opinion of the United States Court of Appeals for the Second Circuit (40-52) is reported in 201 F. 2d 439.

---

* Unless otherwise stated, references in parentheses are to pages of the record.

Jurisdiction

The jurisdiction of this Court is invoked under 28 U. S. C. §1254. The judgment of the Court of Appeals was entered on January 15, 1953 (52). Petition for a writ of certiorari was filed on April 14, 1953 and granted on June 1, 1953. 345 U. S. 969.

Questions Presented

1. In a civil action for damages under Section 12(2) of the Securities Act of 1933 (15 U. S. C. §77 l (2)) was it error for the Court of Appeals to direct, pursuant to Section 3 of the Federal Arbitration Act (9 U. S. C. §3), the enforcement of the parties' agreement to submit their controversy to arbitration?

2. Did the Securities Act of 1933 repeal by implication the Federal Arbitration Act of 1925 as to investors and as to contracts for the purchase and sale of securities?

Statutes Involved

The pertinent provisions of the Securities Act of 1933 are set forth in the brief of the Securities and Exchange Commission. With respect to the Federal Arbitration Act, however, that brief sets forth only Sections 3 and 10, and predicates, upon the language of Section 3, an argument that "the arbitration statute is applicable only to controversies which are properly 'referable to arbitration'" (SEC Br. pp. 12, 26). But this ignores Sections 1 and 2 of the Act which define its coverage and make it universally applicable, excepting only employment contracts.

Sections 1 and 2 of the Federal Arbitration Act (9 U. S. C.) provide as follows:

"§1. 'Maritime transactions' and 'commerce' defined; exceptions to operation of title

"'Maritime transactions', as herein defined, means charter parties, bills of lading of water carriers, agreements relating to wharfage, supplies furnished vessels or repairs to vessels, collisions, or any other matters in foreign commerce which, if the subject of controversy, would be embraced within admiralty jurisdiction; 'commerce', as herein defined, means commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation, but nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce. July 30, 1947, c. 392, §1, 61 Stat. 670."

"§2. Validity, irrevocability, and enforcement of agreements to arbitrate

"A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such

grounds as exist at law or in equity for the revocation of any contract. July 30, 1947, c. 392, §2, 61 Stat. 670."

Statement of the Case

Petitioner is a citizen of the State of New York (2). Respondents are a partnership doing business in New York under the name Hayden, Stone & Co. (7). They are stock-brokers and dealers in securities and with reference to the transactions herein are subject to the Securities Act of 1933. Petitioner brought suit against respondents and another defendant (not involved here) for damages of $3,888.88 under Section 12(2) of the Securities Act of 1933. His complaint (2-4) alleges in substance that on or about January 17, 1951, respondents sold to petitioner 1,600 shares of the common stock of Air Associates, Incorporated, a New Jersey corporation, and that petitioner paid respondent $29,517.54 therefor. The complaint further alleges that said sale was made by means of certain instrumentalities of transportation and communication in interstate commerce and that it

> "was made by means of communications by the defendants to the plaintiff which were and, which included untrue statements of material facts and omitted to state material facts necessary in order to make the statements made in the light of the circumstances under which they were made, not misleading" (Bar. Fifth; 3).

The complaint further alleges that petitioner did not know that the alleged statements were untrue at the time of his purchase of the stock and that petitioner later sold the stock at a loss of $3,888.88.

The transaction between petitioner and respondents was controlled by the terms and conditions of Margin Agreements duly executed by petitioner dated May 2, 1950 and January 18, 1951 (8-9). The agreement of May 2, 1950 opened a separate account in the name of Anthony Wilko and Mary Wilko (16). The agreement of January 18, 1951 opened a separate account in the name of Anthony Wilko alone (22). The agreements were otherwise identical (43 n. 4). The transaction which is the subject of the complaint in this action took place on January 17, 1951 in the joint account. The last paragraph of these agreements, which was directly above the place for petitioner's signature and was in the same size type as the rest of the agreement, provided:

> "Any controversy arising between us under this contract shall be determined by arbitration pursuant to the Arbitration Law of the State of New York, and under the rules of either the Arbitration Committee of the Chamber of Commerce of the State of New York, or of the American Arbitration Association, or of the Arbitration Committee of the New York Stock Exchange or such other Exchange as may have jurisdiction over the matter in dispute, as I may elect. Any arbitration hereunder shall be before at least three arbitrators" (16, 22).

The Court of Appeals noted that petitioner made no claim of "fraud or coercion in procuring his signature to the agreement" (44).

Before answering the complaint, respondents moved (5-6), pursuant to section 3 of the Federal Arbitration Act, 9 U. S. C. §3, for an order staying all proceedings in the

action until an arbitration had been had in accordance with the arbitration provision quoted above. Respondents' motion was made upon the complaint, the affidavit of Sherman M. Bijur, a partner of Hayden, Stone & Co. (7-10), and copies of the margin agreements involved (11-22). These constituted the whole record; petitioner submitted no opposing affidavit (43).

The District Court denied the motion, because it did not "feel that arbitration of the issues at bar is consistent with the policy and language as expressed by Congress in the Securities Act" (32).

The Court of Appeals for the Second Circuit reversed (Judge Clark dissenting). Chief Judge Swan wrote an opinion, in which Judge Chase concurred, holding that "we do not find in the purpose or in the language of the statute, any policy argument strong enough to override the policy of the Arbitration Act" (49). The court also held that the margin agreement was subject to the Securities Act of 1933 and "consequently the arbitrators are bound to decide in accordance with the provisions of section 12(2)" and that "Failure to do so would * * * constitute grounds for vacating the award pursuant to section 10 of the Federal Arbitration Act, 9 U. S. C. A. §10" (48, 49).

SUMMARY OF ARGUMENT

Both the Federal Arbitration Act of 1925 and the Securities Act of 1933 establish important policies of Congress and accomplish important purposes.

"The purpose of that Act [the Federal Arbitration Act] was deliberately to alter the judicial atmosphere pre-

viously existing" which was hostile to arbitration. *Kulukundis Shipping Co.* v. *Amtorg Trading Corp.*, 126 F. 2d 978, 985 (2d Cir. 1942). It establishes that "A written provision in * * * a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction * * * shall be valid, irrevocable and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." Section 2, 9 U. S. C. §2.

Contrary to the argument of the Securities and Exchange Commission (Br. pp. 12, 26), the Arbitration Act affords no room for judicial determination as to whether an issue is referable to arbitration. It is true that Section 3 of the Act prescribes procedure to be followed when an action is commenced "upon any issue referable to arbitration" but that section does not limit Sections 1 and 2 which prescribe that the Act includes all "maritime transactions" and all contracts and transactions involving interstate commerce excepting only "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce."

There is no conflict between the provisions of the Arbitration Act and those of the Securities and Exchange Act of 1933. There is nothing in the latter Act which expressly, or by any reasonable implication, repeals, narrows or limits the plain wording of the Arbitration Act. "The essential purpose of the statute is to protect investors by requiring publication of certain information concerning securities before offered for sale." (*A. C. Frost & Co.* v. *Coeur d'Alene Mines Corp.*, 312 U. S. 38, 40 (1941)).

Under the Act, this purpose is effectuated by requiring the seller to comply with certain provisions of the Act and the regulations promulgated under it with respect to the manner of marketing securities and furnishing information.

The provisions of Section 14 of the Securities Act making void any agreement to waive "compliance" with the Act plainly refer to the seller's "compliance" with the substantive provisions of the Act and not to the buyer's remedies when there has been a failure of compliance on the part of the seller.

In any event, however, an agreement between the buyer and seller to refer a dispute to arbitration does not constitute any waiver at all. The Act created a liability on the part of the seller for any damages sustained by the buyer by reason of an untrue statement of a material fact by the seller or the omission to state material facts, unless the seller can sustain the burden of proof that he did not know and "in the exercise of reasonable care could not have known, of such untruth or omission." It was therefore necessary to provide a forum for this new cause of action. Accordingly, the Act provides that the buyer "may sue either at law or in equity in any court of competent jurisdiction" on this new statutory cause of action. The buyer is thus afforded a statutory cause of action in the federal courts irrespective of diversity of citizenship or jurisdictional amount. In conferring the right to sue in any court of competent jurisdiction at law or in equity, the Act does not limit the remedy to any particular mode of trial. Under the Arbitration Act it is implicit that arbitration is merely a form of trial to be adopted in the action itself in place of the trial at common law, just as actions

are tried before referees or special masters instead of judges and juries. Arbitration was a mode of trial in existence when the Securities Act was adopted, and that statute evidences no intention to alter or repeal it.

Under the heading "Arbitration Cannot Assure the Customer His Statutory Rights" (Br. pp. 30-44) the brief of the Commission marshalls various quotations from texts dealing with the subject of arbitration to suggest that arbitration is of limited value and peculiarly suited to certain limited types of controversies, but this is an argument against the efficacy of arbitration itself—foreclosed by the policy already expressed by Congress in the Federal Arbitration Act.

In urging the informality of the arbitration procedure as a ground for its rejection here, the Commission ignores the fact that arbitrators as a matter of law can decide only the specific controversy referred to them; that the Court of Appeals here has held that the controversy to be submitted to arbitration here shall be that arising under the Securities Act of 1933 including, specifically, the burden imposed by the Act, upon the broker to prove, if there was any misstatement, that he did not know of it, and reasonably could not have known of it; and that the arbitrators' failure or refusal to decide in accordance with this provision would "constitute grounds for vacating the award pursuant to section 10 of the Federal Arbitration Act, 9 U. S. C. A. §10" (48, 49).

The question of law to be decided here is no different than if it were the broker rather than the customer who was trying to escape from his agreement to arbitrate. In

this case, the customer, petitioner, conceives it to be to his interest to go to court rather than to arbitration. In the next case, the situation may well be reversed with the broker resisting arbitration and the customer demanding it. In either case, the question of law is the same.

It is suggested by the Commission (Br. pp. 14, 44) that what is called a "post-controversy" agreement of arbitration would be permissible even though a pre-controversy agreement is contended to be invalid. The Arbitration Act, in Section 2, expressly puts pre-controversy and post-controversy arbitration agreements on precisely the same footing. It validates agreements to arbitrate either "a controversy thereafter arising" or "an existing controversy." The suggestion made therefore would be judicial legislation in its purest form for there is utterly no expression by Congress evidencing any intention to differentiate between them. The very making of the suggestion exposes petitioner's position for what it really is—an attempt to induce this Court to enact legislation which Congress has not.

There is no conflict at all between the two statutes and the decision below properly gives full force and effect to the policies established by Congress in both—allowing both to stand, side by side, with neither encroaching on the other. It affords full recognition and enforcement of rights and liabilities under the Securities Act of 1933. At the same time, it preserves to all parties the right afforded them by the 1925 Act to contract to have those rights and liabilities enforced in the trial forum of their choice, arbitration, without assuming to read into the later enactment provisions which Congress itself neither expressed nor

implied. There is no conflict between the two Acts, or between their respective policies, provisions or objectives.

Throughout the Commission's brief there is constant reiteration of the statement that the arbitration provision, while admittedly appearing directly above the customer's signature, is contained in "a fine-print pre-transaction agreement." Such statements are prefaced, on page 8, with the comment that there "is no indication in the record that the various provisions of the agreement were actually read by the petitioner, or explained to him, before his signature was obtained." There is no indication in the record to the contrary. The record is silent on the subject. Moreover, this is utterly irrelevant to the issue before this Court. The Arbitration Act, by Section 2, specifically preserves to petitioner his rights "upon such grounds as exist at law or in equity for the revocation" of his contract. He is therefore fully protected if he claims the contract to be unenforceable because of fraud, misrepresentation, duress, or for any legitimate reason. When respondent moved here for a stay petitioner made no such claim. Instead, he filed no affidavit at all, but merely contested respondents' motion as a matter of law. From this, as the Court of Appeals observed, "we must assume that the plaintiff [petitioner] voluntarily entered into the agreement and fully understood its terms" (43). The Commission's speculations and its comments upon the size of the type are thoroughly unwarranted in the light of petitioner's own conduct and the language of the statute which afforded him full protection had he chosen to make any such claim himself.

Preservation in securities transactions of the speedy remedy of arbitration, voluntarily selected by the parties, is of great importance in the light of the large volume of such business done in New York City, where delay due to calendar congestion in both state and federal courts is notorious. In the absence of a clear expression from Congress, the Arbitration Act should not be thus foreshortened.

POINT I

The Provisions and Policy of the Securities Act of 1933 Do Not Forbid Arbitration as a Mode of Settling Disputes Arising from an Alleged Violation of Section 12(2) Thereof.

At the outset, we must recognize the "cardinal principle of construction that repeals by implication are not favored. When there are two acts upon the same subject, the rule is to give effect to both if possible." *United States* v. *Borden Co.*, 308 U. S. 188, 198 (1939). See *United States Alkali Export Ass'n* v. *United States*, 325 U. S. 196, 206 (1945). The policy which Congress recognized and favored in 1925 was at least as strong and valid in 1951, when petitioner signed the margin agreement in issue. That Congress happened to recognize and further a policy of another type in 1933, when it passed the Securities Act, cannot affect the 1925 Act in the absence of a clear showing of conflict between the two policies.

The principles of the securities legislation as outlined in the President's message to Congress of March 29, 1933 were summarized thus in H. R. Rep. No. 85, 73d Cong., 1st Sess. 3 (1933):

"* * * In brief, the aims set forth by the President are:

(1) An insistence that there should be full disclosure of every essentially important element attending the issue of a new security.

(2) A requirement that whatever action taken by the Federal Government for such disclosure should be limited to that purpose and should be so devised as not to be capable of being construed as an approval or guarantee of a security issue.

(3) A demand that the persons, whether they be directors, experts, or underwriters, who sponsor the investment of other people's money should be held up to the high standards of trusteeship.

The achievement of these ends is the principal purpose of this bill."

The policy of the Federal Arbitration Act was expressed by the House Judiciary Committee as follows:

"The purpose of this bill is to make valid and enforcible agreements for arbitration contained in contracts involving interstate commerce or within the jurisdiction or [sic] admiralty, or which may be the subject of litigation in the Federal courts. It was drafted by a committee of the American Bar Association and is sponsored by that association and by a large number of trade bodies whose representatives appeared before the committee on the hearing. There was no opposition to the bill before the committee.

* * *

"Arbitration agreements are purely matters of contract, and the effect of the bill is simply to make the contracting party live up to his agreement. He

can no longer refuse to perform his contract when it becomes disadvantageous to him. An arbitration agreement is placed upon the same footing as other contracts, where it belongs.

"The need for the law arises from an anachronism of our American law. Some centuries ago, because of the jealousy of the English courts for their own jurisdiction, they refused to enforce specific agreements to arbitrate upon the ground that the courts were thereby ousted from their jurisdiction. This jealousy survived for so lon [sic] a period that the principle became firmly embedded in the English common law and was adopted with it by the American courts. The courts have felt that the precedent was too strongly fixed to be overturned without legislative enactment, although they have frequently criticized the rule and recognized its illogical nature and the injustice which results from it. The bill declares simply that such agreements for arbitration shall be enforced, and provides a procedure in the Federal courts for their enforcement.

* * *

"In view of the strong support of commercial and legal bodies, the entire lack of opposition before the committee, the obvious justice of the result sought to be attained, and the evident propriety and necessity of Federal action, we submit that the bill should become law. It is practically appropriate that the action should be taken at this time when there is so much agitation against the costliness and delays of litigation. These matters can be largely eliminated by agreements for arbitration, if arbitration agreements are made valid and enforceable."

H. R. Rep. No. 96, 68 Cong., 1st Sess. 1-2 (1924).

The Senate committee said:

> "It has been said that 'arrangements for avoiding the delay and expense of litigation and referring a dispute to friends or neutral persons are a natural practice of which traces may be found in any state of society.' The desire to avoid the delay and expense of litigation persists. The desire grows with time and as delays and expenses increase. The settlement of disputes by arbitration appeals to big business and little business alike, to corporate interests as well as to individuals.
>
> • • •
>
> "The bill, while relating to maritime transactions and to contracts in interstate and foreign commerce, follows the lines of the New York arbitration law enacted in 1920, amended in 1921, and sustained by the decision of the Supreme Court of the United States in the matter of the Red Cross Line v. Atlantic Fruit Co., rendered February 18, 1924."
>
> Sen. Rep. No. 536, 68th Cong., 1st Sess. 3 (1924).

In the face of this, there clearly is no conflict of policy. Nor is there any conflict in the provisions.

The Securities Act imposes upon issuers and sellers of securities certain requirements. Thus, registration statements and prospectuses must contain certain information specified in the Act. Sections 6, 7, and 10, 15 U. S. C. §§77f, 77g, and 77j. These documents are to be filed in the manner and within the times stated. Section 8, 15 U. S. C. §77h. Nor may a seller include an untrue statement or omit a material fact the omission of which might be misleading. Section 12(2), 15 U. S. C. §77*l* (2). With all these require-

ments the broker selling securities must comply. Waiver of compliance is void. Section 14, 15 U. S. C. §77n.

The plain meaning of Section 14 is that the broker cannot secure immunity for himself from complying with the burdens imposed upon him by any agreement with, or waiver by, his customer. The term "compliance with" can only be satisfied by the broker. It is he who must comply with the Act. No duties of compliance whatever are placed upon the customer. Illustrative of a waiver of compliance with the provisions of the Act would be clauses waiving the requirements of a registration statement, or for the delivery of a prospectus or some of the essential items of information listed in the statute. Any waiver of liability for making untrue statements or attempts to shift the burden of proof would be in the same category.

It is plain that the words "waive compliance with any provision" are not the same as "to waive the remedies provided by the Securities Act."

Section 14 makes no mention of waiver of remedies. It does not purport to deal with remedies at all. This is not surprising because good draftsmanship would dictate that separate sections deal with remedies for breach. In fact only in the event of non-compliance with some provision of the Act would the occasion arise for any remedy.

In any event, the Commission's whole argument is predicated upon the proposition that an arbitration agreement is a "waiver" of the right to a suit "at law or in equity." But it is no such thing. It is merely an agreement, made enforceable by statute, as to how any controversy will be procedurally determined at law or in

equity. Here petitioner commenced his suit at law in the Southern District of New York. Respondents invoked Section 3 of the Arbitration Act which prescribes the procedure to be followed thereafter in any such suit where it is made to appear that the parties have agreed to arbitrate the controversy involved—a stay, not a dismissal of the suit: "If any suit * * * be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing * * * the court * * * shall * * * stay the trial of the action until such arbitration has been had * * *." The action is not dismissed. It remains pending. Only the trial is stayed. Instead of proceeding to common law trial it is tried before arbitrators, just as other cases are tried before referees or special masters instead of judges and juries. And the award subsequently made by the arbitrators remains subject to review and vacation by the court in the still pending action.

The realities of the situation were explained by Judge Learned Hand in *Murray Oil Products Co.* v. *Mitsui & Co.*, 146 F. 2d 381, 383 (2d Cir. 1944):

> "In either view therefore § 3 did not need to remove, and did not remove, what would at common law have been a bar; on the contrary, it provided the defendant with relief—a stay—under conditions where before he would have been helpless to assert the arbitration clause at all. This was the measure of its change, so far as we can see; had it meant to go further and finally to dispose of the action, as the defendant argues, it would not have chosen the words used, for a stay presupposes that the action shall not abate; and if it does not, it must go to judgment of one kind or another. If a defendant wins before

> the arbitrators, he must be able to clinch his victory by a judgment; on the other hand, having invoked arbitration, he must also abide the result, if he loses. It would be a lame and impotent conclusion in that event to require the successful plaintiff to begin a new action on the award. Arbitration is merely a form of trial, to be adopted in the action itself, in place of the trial at common law: it is like a reference to a master, or an 'advisory trial' under Federal Rules of Civil Procedure, Rule 39(c), 28 U.S.C.A. following section 723c. That is the whole effect of §3."

In 1925, Congress, by the Arbitration Act, imported into suits at law or in equity the procedure to be followed in such suits where an arbitration agreement existed. It is not a defense or ground of dismissal of the suit. As Judge Hand said, it is merely the prescribed "form of trial, to be adopted in the action itself, in place of the trial at common law."

It is not therefore in any sense a "waiver" of the right to sue at law or in equity—it is only an agreement, sanctioned by Congress, as to the procedure to be followed in the conduct of such suits.

Thus, the whole basis for the Commission's argument (Br. pp. 19-20) falls. Whatever might be the effect if all remedies were waived, it is plain here that there is no waiver at all.

Plainly, too, the permissive words of Section 12(2) of the Act—that, upon non-compliance by the seller, the purchaser "may sue either at law or in equity"—are not mandatory and do not forbid him to seek his damages in

any other manner—such as by settlement or by arbitration. Laws governing venue and jurisdiction, even when apparently affording exclusive jurisdiction to the courts, do not inhibit arbitration.

In *Cavicchi* v. *Mohawk Manufacturing Co.*, 308 U. S. 522 (1939), this Court had before it the policy of the Judicial Code (now 28 U. S. C. §1338), which provided that the jurisdiction of the United States courts should "be exclusive of the courts of the several States * * *" in "all cases arising under the patent-right * * * laws of the United States." A dispute arose as to the validity of a patent, and the parties agreed to submit the dispute to arbitration. The arbitration resulted in an award, which was confirmed under New York law in a state court. The New York Court of Appeals affirmed the order confirming the award, holding that arbitration did not offend the quoted language of the Judicial Code. *Matter of Mohawk Manufacturing Co.* v. *Cavicchi*, 281 N. Y. 629, 22 N. E. 2d 179 (1939). This Court dismissed an appeal for want of a substantial federal question, citing *Red Cross Line* v. *Atlantic Fruit Co.*, 264 U. S. 109 (1924). In the *Red Cross Line* case this Court was urged to vindicate the policy requiring state and federal courts to apply admiralty law uniformly, the requirement of uniformity being implied from the Constitution itself. The New York court had required arbitration of a contract cognizable in admiralty at a time when the federal courts sitting in admiralty would have refused arbitration. This Court held that the policy requiring uniformity in admiralty law was not so all-embracing as to forbid a state from devising its own procedures.

for enforcement of rights, as long as it adhered to the substantive federal law.

At p. 27 the Commission cites a contrary holding in 1930 by the Delaware district court in *Zip Mfg. Co.* v. *Pep Mfg. Co.*, 44 F. 2d 184. Plainly, this case can no longer be regarded as binding. See Robb, *Arbitration Procedure Compared with Court Litigation in Patent Controversies*, 17 Law and Contemp. Prob. 679, 690-1, 693 (1952).

In addition to excluding employment contracts from the scope of federal arbitration, Congress specifically provided in Section 8, 9 U. S. C. §8, that arbitration in admiralty should not prevent "the party claiming to be aggrieved" from beginning "his proceeding hereunder by libel and seizure of the vessel * * *." In *The Anaconda* v. *American Sugar Refining Co.*, 322 U. S. 42 (1944), the owner of a vessel had required of the company to which it was being chartered an arbitration agreement with a clause rendering Section 8 of the Act inapplicable. When a suit between the parties was commenced by a libel against the vessel, the charterer interposed this clause as a defense. This Court held it invalid, 322 U. S. at 46:

> "* * * Congress plainly and emphatically declared that although the parties had agreed to arbitrate, the traditional admiralty procedure with its concomitant security should be available to the aggrieved party without in any way lessening his obligation to arbitrate his grievance rather than litigate the merits in court.
>
> "It is enough that Congress had so declared. We think a party can not stipulate away such a

jurisdiction which the legislation declares open as heretofore."

Clearly, in a statute whose metes and bounds have been so plainly delineated by Congress, there is no room for further drastic limitation by judicial construction of provisions constituting merely a grant of jurisdiction and a broadening of venue.

The Courts of Appeal recognize that provisions in other statutes, even where couched in far more mandatory language than here, are permissive only and do not preclude arbitration.

In the Fair Labor Standards Act (29 U. S. C. §201 *et seq.*) a special statutory penalty was imposed with the provision that an action to recover such liability "may be maintained in any court of competent jurisdiction * * *." The statutory grant of the privilege to resort to any court of competent jurisdiction is identical with that specified in the Securities Act.

The Court of Appeals for the Third Circuit in *Donahue v. Susquehanna Collieries Co.*, 138 F. 2d 3 (3d Cir. 1943), had to deal with a situation almost parallel with that now presented to this Court. There a motion for a stay of trial pending arbitration in accordance with Section 3 of the Federal Arbitration Act was made. There, as here, it was argued that special rights were created by statute which would not lend themselves to arbitration. The court granted the motion for a stay pending arbitration and in its opinion succinctly answered the objections made, saying:

> "Is there anything about the Fair Labor Standards Act which removes claims under its terms

from the arbitration clause? We may concede that Congress could have done so had it wished. It could have provided that any claim under the Act was to be enforced by lawsuit only, notwithstanding any agreement between parties for any other method of settlement. There is no such express language. The plaintiff points to a sentence in the section on 'Penalties; civil and criminal liability' which he contends has the effect just described. 'Action to recover such liability may be maintained in any court of competent jurisdiction * * *' is the language used. We think the effect of this provision is to allow a suitor to proceed in federal court regardless of citizenship of the litigants and amount involved or to sue in a state court at his convenience" (138 F. 2d, at p. 6).

* * *

"No doubt it creates rights which made a basis of a claim by an employee against an employer who violates it. So does any contract. A claim under the Act and a claim based on a contract,—each is based on a legal right which the claimant asserts against someone else. Arbitration is one way by which such a right can be enforced" (138 F. 2d 3, at p. 6).

In *Agostini Bros. Building Corp.* v. *United States*, 142 F. 2d 854 (4th Cir. 1944), an action was brought under the Miller Act (40 U. S. C. §§270a-270d) to recover for labor and materials furnished in the construction of a public building. The defendants sought to stay the federal court action until arbitration could be had pursuant to the terms of the contract. The District Court denied the motion but the Court of Appeals unanimously reversed and directed a stay pend-

ing arbitration. There the statute creating the rights was far more directive than the Securities Act because it prescribed:

> "(b) *Every suit instituted under this section shall* be brought in the name of the United States for the use of the person suing, in the United States District Court for any district in which the contract was to be performed and executed *and not elsewhere,* irrespective of the amount in controversy * * *" (40 U. S. C. §270b (b)) [Emphasis supplied].

Despite this direction, the stay pending arbitration was granted.

In *Watkins* v. *Hudson Coal Co.*, 151 F. 2d 311 (3d Cir. 1945), cert. denied, 327 U. S. 777 (1946), the Court of Appeals held that an action by employees to recover unpaid overtime wages, liquidated damages, reasonable attorneys' fees and court costs under Section 16 of the Fair Labor Standards Act of 1938 (29 U. S. C. §216) was subject to arbitration. In that case the Wage and Hour Division of the United States Department of Labor appeared *amicus curiae,* as the Securities and Exchange Commission has done in the case at bar to urge that arbitration was not applicable. Nevertheless, the court stayed the action pending arbitration.

There is thus nothing in the Act—either in the non-waiver provision or the remedies provision—which expressly or by any reasonable implication can be said to preclude arbitration.

The situation is entirely different from that in *Boyd* v. *Grand Trunk Western Railroad Co.*, 338 U. S. 263 (1949), upon which the Commission relies (Br. pp. 20-22). There

the Act gave the employee a wide choice of venue which, as the Commission concedes, was designed to enable him to pick his jurisdiction so as to include large cities where the amount of his jury verdict would probably be larger. The statute prohibited the carrier from exempting itself "from any liability created by this Act." Federal Employers' Liability Act Section 5, 45 U. S. C. §55. In that case the court could readily take notice on the basis of judicial experience that a waiver of venue could so affect the extent of liability as to constitute a waiver of liability. Apart from the fact that there is no waiver of liability involved here, there would be no reasonable basis for a supposition that arbitration as a mode of trial in this action would affect liability.

Brooklyn Savings Bank v. *O'Neil*, 324 U. S. 697 (1945), is likewise not applicable. The holding there was that an attempted release of the liquidated damages provided for under the Fair Labor Standards Act was invalid because, as Mr. Justice Reed pointed out, ". . . the legislative policy would be thwarted by permitting such contracts." 324 U. S. at 713. The case did not involve a question of statutory construction of either a waiver provision or an arbitration clause.

The fears expressed below and by the Commission (Br. p. 30 *et seq.*) that the burden of proof and other provisions of the Act will not be honored in arbitration, involving as it does a challenge to the integrity and good faith of as yet unchosen arbitrators, reflects to an extent a failure fully to "shake off the old judicial hostility to arbitration," *Kulukundis Shipping Co.* v. *Amtorg Trading Corp.*, 126 F.

2d 978, 985 (2d Cir. 1942). In any event, there is no reason to suppose that arbitration here would be in any way weighted against petitioner. Constant assertion is made that, if arbitration be sustained, petitioner's rights will not be upheld by arbitrators taken from "an industry selected panel." By this the Commission assumes that members of the securities industry, even after they have done business for 20 years under the Securities Act, must necessarily be presumed hostile to it. More importantly it ignores the fact that under the arbitration provision the petitioner himself is given the right to have his claims arbitrated by arbitrators selected from other than the New York Stock Exchange panel. The provision specifically allows petitioner to select either the New York Chamber of Commerce, the American Arbitration Association, or the New York Stock Exchange arbitration rules (16, 22). The American Arbitration Association, for example, favors a lawyer as one of a panel whenever there are, as here, three arbitrators to act. Note, *Predictability of Result in Commercial Arbitration*, 61 Harv. L. Rev. 1022, 1023 n. 12 (1948).

The brief of the Commission (p. 13) asserts:

> "The arbitration process is primarily suited for commercial disputes which often can best be resolved by businessmen on the basis of their own knowledge and experience, and without reference to technical rules of law."

It is suggested (Br. pp. 31, 32) that it is a remedy peculiarly adapted to the disposition of disputes between merchants; that in the securities field it may be a means for settling a variety of technical business disputes; but that where expertise in the law rather than experience in a par-

ticular phase of business is essential to a proper determination of the particular controversy, the arbitration process may be fraught with danger. There is no foundation in fact for these expressions of opinion.

Arbitration has been widely and satisfactorily employed entirely outside the commercial field.

It is a matter of common knowledge that the labor unions have insisted upon and obtained in a great number of major collective bargaining agreements provisions for the compulsory settlement of disputes by arbitration—a plain indication that labor does not feel that arbitration is weighted in favor of business or that its usefulness is confined to commercial disputes. See also 61 Harv. L. Rev. 1027, where the author found it necessary to dispute the contention that arbitration is favorable to the "little man" and 61 Harv. L. Rev. 1031 where it is intimated that in landlord and tenant cases the arbitrators are unduly favorable to tenants rather than landlords.

Finally, the District Court would not confirm an award where the arbitrators are shown to have been actually or potentially biased. See *Stathatos* v. *Arnold Bernstein S. S. Corp.*, 202 F. 2d 525, 526 (2d Cir. 1953); *Petrol Corporation* v. *Groupement d'Achat des Carburants*, 84 F. Supp. 446, 447 (S. D. N. Y. 1949); cf. *Lipschutz* v. *Gutwirth*, 304 N. Y. 58, 106 N. E. 2d 8 (1952).

Arbitrators can readily be requested to follow legal rules. Indeed, in England the arbitrators must decide "according to the legal rights of the parties" (48 n. 9). *Jager* v. *Tolme & Runge*, [1916] 1 K. B. 939, 953 (C. A.); *Czarnikow* v. *Roth, Schmidt & Co.*, [1922] 2 K. B. 478, 484 (C. A.); *Stotesbury* v. *Turner*, [1943] K. B. 370.

What Lord Justice Bankes said in the *Czarnikow* case is apposite. He said, [1922] 2 K. B. at 484:

> "Among commercial men what are commonly called commercial arbitrations are undoubtedly and deservedly popular. That they will continue their present popularity I entertain no doubt, so long as the law retains sufficient hold over them to prevent and redress any injustice on the part of the arbitrator, and to secure that the law that is administered by an arbitrator is in substance the law of the land and not some home-made law of the particular arbitrator or the particular association. To release real and effective control over commercial arbitrations is to allow the arbitrator, or the Arbitration Tribunal, to be a law unto himself, or themselves, to give him or them a free hand to decide according to law or not according to law. • • • Unlimited power does not conduce to reasonableness of view or conduct."

The Commission seeks to weaken the effect of the English cases by asserting (Br. p. 29) that even apart from statute the English courts had refused to enforce arbitration of fraud cases. The authorities cited (Br. p. 29 n. 20) for this proposition do not support it. Both the *Wallis* and *Workman* cases cited are holdings only that the particular controversies involved did not come within the scope of the arbitration agreement as written. There is some language in the *Workman* case in regard to the effect of fraud but it clearly does not stand for the broad proposition for which it is cited by the Commission. The *Green* case involved an election of remedies where the party seeking arbitration had gone to court instead of requesting arbitration within a three day limitation provided for in the agreement. In

any event, the cases would not be in point because under the law of England as it stood when they were decided, the English courts, unlike our courts under the Arbitration Act, had discretion as to whether to stay proceedings pending arbitration. Thus in the *Barnes* case, cited in the Commission's footnote, the Court said, [1898] 1 Ch. at 417:

> "In matters of this kind—motions to stay proceedings by reason of an agreement to refer to arbitration—the Court undoubtedly has a discretion—a judicial discretion of course. In the present case, looking at the circumstances, I think in exercising my judicial discretion I ought not to order a stay of proceedings."

At Br. p. 36, the Commission refers to certain provisions of the English Arbitration Act under which the court at the request of the arbitrator can make rulings on questions of law during the course of the arbitration. The same result has already been obtained here. Under the ruling below the arbitrators are required to determine, if any misstatements of fact were made by the seller, whether the seller can sustain the burden of proving that it did not know and could not in the exercise of reasonable care have known of the misstatements. In other words, here the Court has already ruled and laid down the principles of law which must and will govern the arbitration.

We know of no case in this country which holds that arbitrators may not be required, by the terms of the submission, to follow legal standards. On the contrary, there are many instances of arbitrators being required to decide in accordance with a specific statute or in accordance with

a standard set forth in the submission agreement. *Campbell* v. *American Fabrics Co.*, 168 F. 2d 959, 962 (2d Cir. 1948); *Evans* v. *Hudson Coal Co.*, 165 F. 2d 970, 974 (3d Cir. 1948); *Columbian Fuel Corporation* v. *United Fuel Gas Co.*, 72 F. Supp. 843, 844-45 (S. D. W. Va. 1947), aff'd, 165 F. 2d 746 (4th Cir. 1948); *Watkins* v. *Hudson Coal Co.*, 151 F. 2d 311, 313, 321 (3d Cir. 1945), cert. denied, 327 U. S. 777 (1946); *Toledo S. S. Co.* v. *Zenith Transp. Co.*, 184 Fed. 391, 392, 395 (6th Cir. 1911). ". . . whether the arbitrator shall hear the case according to rules of the law of evidence and/or according to substantive law, depends upon the agreement of the parties; they may agree that one or more of those rules shall apply." Dean Wesley A. Sturges, address before the Association of the Bar of the City of New York (74 Reports, Association of the Bar, 1941).

Judge Goodrich was blunt on this point in *Watkins* v. *Hudson Coal Co.*, where he ruled, 151 F. 2d at 313:

> "Our conclusion is that the matter should proceed to arbitration, but only in accordance with the rulings of law as hereinafter set out."

The New York courts consider it a matter of course that arbitrators must decide in accordance with law if the submission so provides. See *Matter of Springs Cotton Mills (Buster Boy Suit Co.)*, 275 App. Div. 196, 200, 88 N. Y. S. 2d 295 (1st Dep't), aff'd, 300 N. Y. 586, 89 N. E. 2d 877 (1949); cf. *Tarello* v. *John A. Johnson Contracting Corporation*, 50 N. Y. S. 2d 212 (not officially reported) (Sup. Ct.), aff'd, 268 App. Div. 893, 51 N. Y. S. 2d 87, leave to appeal denied, 268 App. Div. 903, 51 N. Y. S. 2d 640 (1st Dep't 1944), 294 N. Y. 646, 68 N. E. 2d 523 (1945).

As a matter of fact, such evidence as there is indicates that arbitrators tend to follow the law. The *Harvard Law Review* studied about 300 unpublished decisions under the rules of the American Arbitration Association rendered from October 1946 through December 1947, and reached this conclusion, Note, *Predictability of Result in Commercial Arbitration*, 61 Harv. L. Rev. 1022, 1024 (1948):

> "The awards of arbitrators show rather close adherence to the rules of substantive law insofar as law can be isolated from fact or procedure. This is clearly so where the ethical notions underlying such rules appeal to a layman. No one need explain to an arbitrator the social utility of enforcing contractual obligations, in order to convince the arbitrator that a breach of contract should be compensated. But where the ethical notions underlying rules of law have little or no appeal in a particular business context, arbitrators may disregard the legal rule. Consequently the lawyer must test the 'law' applicable to the case by his knowledge of business ethics and trade custom. This leaves for the lawyer the task of determining when the moral basis of the applicable law is too weak to compete with ethical business notions not relevant in a court. But this is a far cry from saying that anything can happen in arbitration."

Nor is there any basis for holding that the underlying policy of the Act, or the nature of the arbitration process, requires any different conclusion.

In enacting the Securities Act, Congress was not dealing with arbitration but with the evils created by the failure to give accurate or adequate information to the purchaser

of securities. There was no finding or even supposition that the public had failed to receive proper redress from sellers of securities because of arbitration or arbitration agreements. In all the investigations by congressional committees of fraudulent and deceptive practices to which purchasers of securities were subject (see, *e.g.*, *Stock Exchange Practices*, Sen. Rep. No. 1455, 73d Cong., 2d Sess. 5-81 (1934)), there is no showing that arbitration agreements had been used or were even thought of as instruments of oppression. No facts were presented and there was no debate upon the subject tending to show that claims arising from misrepresentation of facts in connection with security transactions must be brought exclusively in the courts and the parties deprived of recourse to any other forum.

When Congress passed the Securities Act, the Arbitration Act had been in existence for eight years and provided, where the parties had agreed upon arbitration, for a stay pending arbitration. By 1933 many of the states had passed arbitration statutes and the courts had sustained arbitration agreements. This being the situation, had Congress wished to take away all rights of arbitration with respect to security transactions it would have been a simple matter so to provide. But Congress made no such provision.

We have pointed out at the outset the manifest error underlying the Commission's whole argument (Br. p. 26 *et seq.*) which is predicated upon a misconception of the language contained in Section 3 of the Arbitration Act. The scope of the statute is defined by Sections 1 and 2 and is all inclusive, except for employment contracts.

The cases cited in further support of the argument are likewise inapposite. As we have shown, the *Zip* case, cited on page 27, is no longer the law since this Court's decision in the *Cavicchi* case, *supra* p. 19. *Matter of Kingswood Management Corp.* (*Salzman*), 272 App. Div. 328, 70 N. Y. S. 2d 692 (1st Dep't 1947), involved a cause of action for treble damages for overcharges of rent made actionable by the Federal Emergency Price Control Act of 1942 which had been settled by stipulation and entry of judgment in the Municipal Court. This stipulation provided that the matter of attorney's fees should be arbitrated. The Court ruled that since the right to recover attorney's fees was created by a provision of the Act allowing "reasonable attorney's fees and costs *as determined by the court*" (emphasis supplied), any such award must be made by the court which heard the case and which was, therefore, "in the best position to appraise the value of the attorney's services" (272 App. Div. at 330). The Court emphasized that:

> "Power to determine the attorney's fee is incidental to the determination of the action, and can only be exercised in the forum which has jurisdiction thereof" (*id.* at 331).

The statutory remedy in the *Kingswood* case, in terms extending only to fees determined by the same court that heard the treble damage action, was thus quite different from the statutory remedy provided by Section 12(2) of the Securities Act of 1933 (15 U. S. C. §77*l*(2)). Beyond the provision that the person damaged might sue either at law or in equity in any court of competent jurisdiction, there is nothing in the substantive language of that section mak-

ing the determination of the issue one peculiarly within the province of any single court.

In *Application of Diamond*, 80 N. Y. S. 2d 465 (not officially reported) (Sup. Ct.), aff'd, 274 App. Div. 762, 79 N. Y. S. 2d 924 (1st Dep't 1948), the decision merely was that in a stockholder's derivative suit an arbitration agreement contained in a contract between the corporation's stockholders was inapplicable to the controversy involved. *Application of Cohen*, 183 Misc. 1034, 52 N. Y. S. 2d 671 (Sup. Ct. 1944), aff'd, 269 App. Div. 663, 53 N. Y. S. 2d 467 (1st Dep't 1945), leave to appeal denied, 269 App. Div. 690, 54 N. Y. S. 2d 389, 294 N. Y. 640, 61 N. E. 2d 459 (1945), involved a construction of an arbitration agreement between the stockholders providing for arbitration of controversies involving "the conduct of the business." The Court held that this agreement plainly did not apply in a statutory proceeding for dissolution of the corporation where the stockholders were deadlocked. Obviously, the sovereign right of control, and its governmental interest in, the matter of custody of children and the distribution of decedents' estates would forbid such matters' being relegated to private arbitration, which was all that was held in *Hill* v. *Hill*, 199 Misc. 1035, 104 N. Y. S. 2d 755 (Sup. Ct. 1951), and *Swislocki* v. *Spiewak*, 273 App. Div. 768, 75 N. Y. S. 2d 147 (1st Dep't 1947). The *Quarrington Court* case, Br. p. 28, 102 F. 2d 916 (2d Cir.), cert. denied, 307 U. S. 645 (1939), merely held that a ship owner could not seek piecemeal determination by arbitration with one of several parties involved in a plenary limitation proceeding which he himself had commenced joining all interested parties.

There is, on the face of the statute and the existing authorities, no basis therefore for selecting any kind of contracts or transactions as being outside the scope of the Arbitration Act where, as here, Congress has given no indication whatever that such was its intention.

CONCLUSION

The judgment below should be affirmed.

Respectfully submitted,

HORACE G. HITCHCOCK,
Attorney for Defendants-Respondents.

RALPH D. RAY,
FRANCIS E. KOCH,
Of Counsel.